[JOINT COMMITTEE PRINT]

SUMMARY OF TAX AND SPENDING REDUCTION PROVISIONS (WITHIN THE JURISDICTION OF THE COMMITTEES) ON WAYS AND MEANS AND FINANCE OF H.R. 4170 AS PASSED BY THE HOUSE AND THE SENATE

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of the

JOINT COMMITTEE ON TAXATION,
COMMITTEE ON WAYS AND MEANS,
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INTRODUCTION

This pamphlet provides a summary of the tax and spending reduction provisions (within the jurisdiction of the House Committee on Ways and Means and the Senate Committee on Finance) of H.R. 4170 as agreed to by the conferees, and as passed by the House and the Senate on June 27, 1984. (H. Con. Res. 328, to provide technical and clerical corrections to H.R. 4170, was passed by the House on June 27, 1984, amended and passed by the Senate on June 29, 1984, and approved by the House as amended on June 29, 1984.) The tax provisions (titles I-X) make up Division A of the Conference Report (Tax Reform Act of 1984). The spending reduction provisions in Division B within the jurisdiction of both the Ways and Means and Finance Committees are the Medicare provisions of title III and title VI (OASDI, SSI, AFDC, and Other Programs). In addition, the medicaid, maternal and child health and Hill-Burton Fund provisions of title III are within the jurisdiction of the Finance Committee.

The first part of the pamphlet, prepared by the staff of the Joint Committee on Taxation, is a summary of the Tax Reform Act of 1984. The second part of the document is a summary of the Medicare, OASDI, SSI, AFDC, trade and other programs of Division B, and is prepared by the staff of the Ways and Means Committee.

Part three is a summary, prepared by the staff of the Finance Committee, of the medicaid, maternal, child health, and Hill-Burton Fund provisions of Division B.

The Appendix presents estimated budget effects of the tax provisions and of the above-mentioned spending provisions.

PART ONE: SUMMARY OF TAX REFORM ACT OF 1984

(Division A: Titles I–X)

I. TAX FREEZE; TAX REFORMS GENERALLY

A. Tax Freeze and Related Provisions

1. Investment credit for used property

Under present law, the maximum amount of used property eligible for the investment credit is scheduled to increase from $125,000 to $150,000 in 1985. The conference agreement freezes the amount eligible for the credit at $125,000 through 1987, after which this limit increases to $150,000.

2. Finance leasing

Under present law, liberalized leasing rules for agreements relating to limited use property or containing fixed price purchase options become effective on January 1, 1984. The conference agreement postpones that effective date for four years. Prior to the new effective date, present liberalized leasing rules are allowed for certain cogeneration facilities and automotive manufacturing property and are continued for up to $150,000 of farm equipment per lessee. In addition, general transitional rules are provided.

3. Expensing of business personal property

Under present law, the amount of personal property which businesses may elect to expense each year is scheduled to increase from $5,000 in 1983 to $7,500 in 1984 and 1985 and to $10,000 thereafter. The conference agreement freezes the maximum amount that can be expensed at $5,000 through 1987, increasing it to $7,500 in 1988 and 1989 and $10,000 thereafter.

4. Cost-of-living adjustments in pension plan limitations

TEFRA reduced the overall dollar limits on contributions and benefits under qualified pension, profit-sharing, and stock bonus plans (qualified plans). In addition, TEFRA suspended all cost-of-living adjustments to these dollar limits through 1985. Beginning in 1986, the limits will be adjusted for post-1984 cost-of-living increases under the formula then in effect to provide cost-of-living increases in social security benefits.

Under the conference agreement, cost-of-living adjustments are postponed until 1988.

5. Net interest exclusion

Under present law, starting in 1985, individuals may exclude 15 percent of interest income to the extent such income exceeds certain interest deductions, up to a maximum exclusion of $450 for single persons and $900 for married couples. The conference agreement repeals this net interest exclusion.

6. Foreign earned income exclusion

Under present law, the maximum amount of income earned abroad that is excludible from an individual's taxable income is $80,000 for 1983. This amount is scheduled to increase in $5,000 annual increments to a permanent level of $95,000 in 1986. The conference agreement freezes the amount of the exclusion at $80,000 through 1987 and thereafter increases it annually in $5,000 increments to $95,000 by 1990.

7. Maximum estate and gift tax rate

Under present law, the maximum estate and gift tax rate is 55 percent in 1984 and is scheduled to decline to 50 percent in subsequent years. The conference agreement freezes the maximum rate at 55 percent through December 31, 1987, and reduces the rate to 50 percent in 1988 and thereafter.

8. Windfall profit tax rate on newly discovered oil

Under present law, the rate of windfall profit tax on newly discovered oil is scheduled to fall from 25 percent for 1983 to 22.5 percent for 1984, 20 percent for 1985, and 15 percent thereafter. The conference agreement provides that this tax rate is 22.5 percent for 1984 through 1987, 20 percent for 1988, and 15 percent thereafter.

9. Percentage depletion on secondary and tertiary production

Under present law, the allowance for percentage depletion on secondary and tertiary oil production expired at the end of 1983. The conference agreement corrects the technical error leading to this termination and clarifies that percentage depletion will not be available after 1983 for secondary or tertiary production from proven properties transferred after 1974.

10. Telephone excise tax

Under present law, the 3-percent telephone excise tax is scheduled to expire after 1985. Under the conference agreement, the 3-percent tax remains in effect through 1987.

11. Excise tax on distilled spirits

Under present law, the excise tax on distilled spirits is $10.50 per proof gallon. The conference agreement increases the tax to $12.50 per proof gallon after September 30, 1985. The conference agreement also imposes a floor stocks tax on previously taxed distilled spirits held for sale on October 1, 1985. A *de minimis* exception from the floor stocks tax is provided for small retail and wholesale dealers, and an installment payment schedule is available to middle-sized dealers.

12. Modification of manner of paying tobacco and alcohol product excise taxes

The conference agreement requires taxpayers who were liable for $5 million or more in any tobacco or alcohol product excise tax in the preceding calendar year to pay that tax during the succeeding calendar year by electronic funds transfer to a Federal Reserve Bank. This provision applies to payments due on and after September 30, 1984.

B. Leasing Provisions

1. Tax-exempt entity leasing

The Federal income tax benefits of ownership of property generally include accelerated depreciation deductions and investment tax credits. Essentially, the law is that the economic substance of a transaction, not its form, determines who is entitled to the tax benefits associated with ownership. Thus, in a lease or similar arrangement, the person claiming ownership for Federal income tax purposes must show that he has sufficient economic indicia of ownership.

The tax benefits of ownership are generally allowed only for property used for a business or income-producing purpose. They are not available for property that is owned by governmental units and tax-exempt organizations. Property that is used (though not owned) by a tax-exempt organization or a domestic governmental unit qualifies for accelerated cost recovery (ACRS) or other depreciation deductions but generally does not qualify for investment credits. A statutory exception to the investment credit limitation provides that qualified rehabilitation expenditures for a building leased to a tax-exempt organization or a governmental unit can qualify for the rehabilitation tax credit. Also, one court has held, and the Internal Revenue Service (IRS) has ruled, that investment credits can be taken where a governmental unit essentially contracts not for the use of property itself, but rather for a service to be provided by the owner of the property.

Property used by a foreign government or person is not subject to the nontaxable use restriction. However, if the property is used predominantly outside the United States, generally ACRS deductions are slowed down and no investment credit is allowed.

Only 50 percent of the investment credit otherwise allowable is allowable with respect to property owned by a thrift institution, but no such limitation specifically applies with respect to property leased to it. Furthermore, certain property owned by or leased to a public utility is subject to special depreciation and investment credit rules. However, those rules are not specifically applicable to property used to provide services to the public utility.

In general, the conference agreement reduces the tax benefits available for certain property that is used by tax-exempt entities. Under the bill, tax-exempt entities include the United States, any State or local governmental unit, possessions of the United States, and most agencies and instrumentalities of any of the foregoing. The term also includes (1) organizations (other than farmers' cooperatives described in section 521) exempt from United States income tax and certain formerly exempt organizations, and (2) certain foreign persons or entities.

The conference agreement generally requires that ACRS or other depreciation deductions for that portion of tangible property leased to tax-exempt entities be computed using the straight-line method over a recovery period equal to the greater of the present class life of the property under the Asset Depreciation Range system (40 years in the case of real property), or 125 percent of the term of the lease. In the case of real property, this provision applies to the extent of use of a type or types specified in the bill, but only if more than 35 percent of the property is so used. The depreciation rules of the conference agreement do not apply to certain short-lived property.

The conference agreement also provides criteria for determining whether a transaction that is structured as a service contract or other arrangement (other than with respect to certain low-income housing) should be treated as a lease for all Federal income tax purposes. Special service contract rules are provided for certain solid waste disposal, energy, and clean water facilities. The rehabilitation credit will be denied for tax-exempt use real property. Finally, lessors generally will not be entitled to investment credits with respect to property leased to thrift institutions in excess of the credits that would have been allowed to the lessee had the lessee owned the property.

The conference agreement does not apply to property leased to a tax-exempt entity for a short term. For depreciation purposes, a short-term lease is generally a lease with a term less than 1 year or less than 30 percent of the property ADR mid-point life (to the extent that life does not exceed 10 years). For investment credit purposes, a short-term lease is generally a lease of less than 6 months, although for certain property, the depreciation short-term lease rule applies.

The conference agreement generally applies to property placed in service by the taxpayer after May 23, 1983, and to property used under an agreement entered into after that date. However, transitional rules are provided.

2. Motor vehicle operating leases

Leases of motor vehicles often contain terminal rental adjustment clauses (TRACs). A TRAC passes on to the lessee the risk that the vehicle will be worth less at the end of the lease term than the parties projected when the lease was entered into. Under present law, it has been held that an agreement with a TRAC in it does not qualify as a lease for Federal income tax purposes.

Under the conference agreement, TRACs are to be disregarded in determining whether certain motor vehicle agreements with respect to property which the lessee intends to use for business purposes qualify as leases for Federal income tax purposes. However, no lessee can be treated as the tax owner of property subject to such an agreement.

The provision is effective for transactions entered into 90 days after the date of enactment.

C. Treatment of Bonds and Other Debt Instruments

1. Debt obligations acquired at a discount

a. Market discount

Under present law, upon the disposition of a market-discount bond issued by a corporation or a governmental unit and held for more than one year, capital gain treatment is accorded to the appreciation in value attributable to market discount. When a taxpayer borrows the funds used to purchase a market-discount bond, interest on the acquisition indebtedness generally can be deducted currently against ordinary income. Thus, a taxpayer who leverages the purchase of a market-discount bond effectively converts ordinary income to capital gain.

The conference agreement generally requires that gain on disposition of a market discount bond be recognized as interest income, to the extent of accrued market discount. This provision is effective for bonds issued after the date of enactment.

The conference agreement also limits a taxpayer's ability to take current interest deductions on indebtedness incurred to purchase or carry a market discount bond. This change is effective for bonds acquired after the date of enactment. For bonds issued before date of enactment but acquired after date of enactment, gain will be recharacterized as ordinary income to the extent of deferred interest deductions.

The conference agreement provides an election to include accrued market discount in income currently. Neither the rule requiring ordinary income treatment on disposition nor the rule limiting interest deductions will apply to bonds with respect to which the election is made.

b. Original issue discount on tax-exempt bonds

Under the Code, original issue discount (OID) on certain obligations issued by a State or local government is exempt from tax. Under Internal Revenue Service rulings, tax-exempt OID is apportioned on a straight-line basis among the original holder and subsequent purchasers of a bond. The application of this rule may permit the holder of a deep discount municipal bond to generate an artificial loss by disposing of the bond prior to maturity.

The conference agreement requires the holders of tax-exempt obligations to accrue tax-exempt OID by using the constant interest method provided by present law for the holders of obligations issued by corporations and other entities. Under the conference agreement, the basis of an obligation is increased by the amount of accrued tax-exempt OID. Thus, the holder of a zero coupon municipal bond will be able to claim economic losses realized on disposition of the bond. These changes apply to bonds issued after September 3, 1982, and acquired after March 1, 1984.

c. Discount on short-term obligations

For governmental obligations (Treasury bills) issued at a discount and payable without interest at a fixed maturity not exceeding one year, the acquisition discount is not considered under present law to accrue until the obligation is paid at maturity or otherwise disposed of. A similar rule applies with respect to original issue discount on other obligations with a maturity of one year or less (e.g., bank certificates of deposit). Taxpayers who make leveraged purchases of obligations eligible for the special rules are able to defer tax liability on unrelated income.

The conference agreement limits the scope of the special rules permitting deferral of discount income on these short-term obligations. Accrual basis taxpayers and certain cash basis taxpayers including those who hold Treasury bills and short-term original discount obligations for sale to customers will be required to account for the discount on an accrual basis. Taxpayers may elect to treat this change as a change in method of accounting and space the payment of any net tax liability over 5 years. The conference agreement also limits the ability to use leveraged purchases of short-term obligations within the special rules to defer tax on ordinary income by deferring the deductions for interest on indebtedness used to purchase or carry short-term discount obligations. An election is provided under which taxpayers who remain eligible for the special rules can avoid application of the interest deferral rule by electing to include acquisition and original issue discount in income as it accrues.

This provision is effective for obligations acquired after the date of enactment.

D. Corporate Tax Provisions

1. Dividends received by corporations

a. Debt-financed portfolio stock

Under present law, when a corporation borrows funds used to purchase dividend-paying stock, interest on the acquisition indebtedness is generally deductible against ordinary income. Dividends received by a corporation are eligible for an 85-percent dividends received deduction.

Under the conference agreement, the dividends received deduction is generally reduced by an amount determined by reference to interest paid or accrued on debt that is directly attributable to investment in the underlying stock. Certain regulatory authority is granted.

The provision applies to stock the holding period for which begins after the date of enactment.

b. Dividends from regulated investment companies

Under present law, a mutual fund, or regulated investment company (RIC), is not subject to Federal income tax if it distributes its income to its shareholders. If at least 75 percent of a RIC's gross income consists of dividends from domestic corporations, then the entire amount of the RIC's dividends to its shareholders is eligible for the 85-percent intercorporate dividends received deduction and the $100 dividend exclusion for individuals.

Under the conference agreement, the 75-percent rule of present law is raised to 95 percent (100 percent for corporate shareholders). Technical changes are also made.

The provision applies with respect to taxable years of a RIC beginning after the date of enactment.

c. Extraordinary dividends and holding period

Under present law, dividends received by a corporation generally have no effect on its basis in the stock of the distributing corporation.

Under the conference agreement, if a corporate shareholder does not hold stock for more than one year, the fair market value of any extraordinary dividend (to the extent not subject to tax) reduces its basis in the stock. Extraordinary dividends include dividends received within any 85-day period with a fair market value equal to or greater than 10 percent (5 percent in the case of preferred stock) of the taxpayer's basis in the stock. This change applies to distributions after March 1, 1984.

Under present law, the dividends received deduction is allowed generally only if a 15-day holding period requirement is satisfied. The holding period is limited to exclude certain periods during which the taxpayer has sold short substantially identical stock or purchased a put option. The conference agreement extends the general holding period requirement to 45 days. It also excludes any period during which the taxpayer is the grantor of a deep-in-the-money option with respect to the stock and any period that the taxpayer's risk of loss is diminished because of holding substantially similar or related positions. This holding period provision applies to stock acquired after the date of enactment.

A corporate shareholder's holding period for certain property received in a distribution is amended. This change applies with respect to distributions after the date of enactment.

2. Ordinary nonliquidating dividends of appreciated property

Generally, under present law, a distribution of appreciated property by a corporation with respect to its stock is not a taxable event to the distributing corporation.

Under the conference agreement, in general, an ordinary, nonliquidating distribution of appreciated property is taxable to the distributing corporation. Certain exceptions are provided. The provision generally applies with respect to distributions declared on or after June 14, 1984.

The provision does not apply to distributions before 1985 to certain 80-percent corporate shareholders. Transitional rules are also provided.

3. Transactions in mutual fund shares

Under present law, mutual fund distributions from net capital gain income are taxed as long-term capital gain to shareholders even when made to a shareholder who holds the share for one year or less. If a shareholder who has held a share of a mutual fund for less than 31 days sells such share at a loss after a capital gain dividend has been received, the loss is treated as long-term rather than short-term to the extent of the capital gain dividend. Similar rules apply to real estate investment trusts.

Under the conference agreement, losses on mutual fund stock held 6 months or less are treated as long-term losses to the extent of any capital gain dividends paid on the stock. There is an exception for periodic redemption plans. A similar rule is provided for real estate investment trusts.

The provision applies to losses with respect to shares of stock with respect to which the taxpayer's holding period begins after the date of enactment.

4. Expenses incurred in connection with short sales

A short sale is a transaction in which the investor borrows stock, sells the stock, and later buys stock to repay the loan. Under present law, amounts paid by the taxpayer to the lender in lieu of dividends are deductible against ordinary income. A taxpayer can create short-term capital gain and ordinary loss by selling short before a dividend payment date and closing the short sale after the ex-dividend date in a transaction with essentially no economic consequences.

Under the conference agreement, in the case of a short sale of stock, payments in lieu of dividends are not deductible, to the extent they exceed amounts received as compensation for the use of collateral for property borrowed in connection with the short sale, unless the short sale is held open for at least 46 days. No deduction is allowed for payments in lieu of extraordinary dividends unless the short sale is held open for more than one year. Where the taxpayer's risk of loss is reduced from holding other positions, the rules applicable to the holding period requirement for the dividends received deduction apply. In addition, a short sale is treated as debt, and short sale expenses not capitalized are treated as interest, for purposes of Code rules limiting the deduction of investment interest or disallowing interest applicable to tax-exempt obligations.

The provision applies with respect to short sales after the date of enactment.

5. Transactions in stock warrants

Present law is unclear as to the tax consequences of a corporation's dealing in its own warrants. Under present law, taxpayers with a gain may take the position that no gain is recognized and taxpayers with a loss may report the loss.

Under the conference agreement, no gain or loss is recognized by a corporation on any transaction with respect to a warrant to buy or sell its own stock. The provision applies with respect to warrants acquired or lapsing after the date of enactment.

6. Companies that accumulate earnings

Under present law, a corporation may deduct 85 percent of the dividends it receives on portfolio stock investments. Furthermore, gain on the sale of stock held by an individual for more than one year is generally taxed as long-term capital gains at rates not in excess of 20 percent. As a result, if a widely held investment company invests in dividend-paying stocks and pays no dividends, its shareholders could hold the stock for at least a year and then sell it at a price that reflects dividends received and retained by the company. Their gains would generally be long-term capital gain, so individual shareholders would essentially be recognizing dividend income at a tax rate substantially below 50 percent. The company may take the position that it is not subject to the accumulated earnings tax because it is widely held.

Under the conference agreement, generally, widely held companies (including operating companies) are not automatically excluded from the accumulated earnings tax. Also, the net capital loss deduction (including by carryover) is denied for mere investment or holding companies and amended, along with other provisions, for other companies.

These provisions apply with respect to taxable years beginning after the date of enactment.

7. Distribution of debt by a corporation

Under present law, earnings and profits of a corporation are probably reduced by the principal amount of its obligations distributed to shareholders. Generally, for noncorporate shareholders, the amount of a distribution taken into account is the fair market value of the property distributed. A long-term obligation bearing little or no stated interest will have a fair market value well below its stated redemption price. The result may be to eliminate corporate earnings and profits at the cost of a relatively small dividend to shareholders.

The conference agreement amends the earnings and profits rules to limit the reduction in earnings and profits resulting from the distribution of the corporation's own debt obligations. Also, under the bill, these obligations are subject to the original issue discount rules.

These provisions apply with respect to distributions declared after March 15, 1984.

8. Phaseout of graduated rates for large corporations

Under present law, the first $100,000 of corporate taxable income is taxed at graduated rates. The taxable income in excess of $100,000 is taxed at the 46-percent rate. The graduated tax rates provide a tax reduction of $20,250 to corporations with taxable income in excess of $100,000 relative to a flat 46-percent tax.

The conference agreement provides that the benefits of the graduated rates will be phased out for any corporation with taxable income in excess of $1 million. An additional 5-percent tax, not to exceed $20,250 in amount, will be imposed on a corporation's taxable income in excess of $1 million. This provision will be effective for taxable years beginning after December 31, 1983.

9. Corporate tax preferences

Under present law, the following corporate tax preferences are reduced by 15 percent: special recapture rules for sales of real property; percentage depletion for coal and iron ore; DISC; amortization of pollution control facilities; bad debt reserves of financial institutions; interest with respect to tax-exempt securities owned by financial institutions; intangible drilling costs of major oil companies; and mineral exploration and development costs.

The conference agreement increases the present law corporate tax preference cutback (other than for coal and iron ore depletion) from 15 percent to 20 percent, beginning in 1985, including applying the increased cutback to the new foreign sales corporation provisions in lieu of DISC.

10. Golden parachutes

Under the conference agreement, certain payments under "golden parachute" or similar contracts substantially in excess of historic compensation will be presumed not to be reasonable compensation and not deductible. Furthermore a nondeductible 20-percent excise tax will be imposed on the recipient. The presumption will be rebuttable.

The provisions are generally effective with respect to payments under contracts entered into after June 14, 1984.

11. Earnings and profits

Distributions from a corporation are generally treated as dividends only if they are paid out of current or accumulated earnings and profits. Under present law, a corporation's earnings and profits may be substantially less than its "true," or economic, income. This is because many of the tax rules applicable in determining taxable income are applicable to a greater or lesser extent in determining earnings and profits.

The conference agreement makes a number of changes in the definition of earnings and profits in order to make them conform more closely to true or economic income. Special rules are provided for distributions to certain 20-percent corporate shareholders. The conference agreement also makes provision for the effect on earnings and profits of redemptions. With exceptions, the provisions are effective after September 30, 1984.

12. Net operating losses

Provisions from the Tax Reform Act of 1976 relating to special limitations on the carryover of net operating losses and other tax attributes are scheduled to become effective at varying times during 1984.

The conference agreement delays the effective date of those provisions, generally until 1986. As a result, the rules in effect prior to 1984 remain in effect.

13. "C" reorganizations

Present law contains no requirement that the transferor corporation distribute all its assets to shareholders in order for a transaction to qualify as a "C" reorganization.

The conference agreement requires the transferor corporation to distribute all its assets to shareholders in order to qualify a transaction as a "C" reorganization. The Treasury is authorized to prescribe regulations providing relief from the rules in appropriate cases. The conference agreement also requires an appropriate allocation of earnings and profits in certain "C" and "D" reorganizations.

The provisions are effective for transactions pursuant to a plan adopted after the date of enactment.

14. "D" reorganizations

Under present law, the transfer of assets of a corporation to another corporation qualifies as a non-divisive "D" reorganization if, among other things, shareholders of the acquired corporation are in control of the acquiring corporation immediately after the transaction. Control is defined as ownership of at least 80 percent of the total combined voting power of all classes of stock entitled to vote and at least 80 percent of the total number of all other classes of stock.

The conference agreement changes the control requirement applicable to non-divisive "D" reorganizations. The provisions apply to transactions pursuant to a plan adopted after the date of enactment.

15. Collapsible corporations

In general, under present law, a collapsible corporation is one which is formed or availed of with a view (on the part of those in control of the corporation) to realize the value of the corporation's collapsible assets before the corporation has realized a "substantial part" of the taxable income to be derived from such property. Under the conference agreement, the substantial part requirement is defined to be "two-thirds" of the taxable income to be derived from the property.

The "70/30" rule of present law is amended to authorize Treasury regulations specifying the extent to which all inventory assets are to be aggregated and treated as a single asset in determining whether the gain attributable to such assets should be treated as attributable to collapsible assets for purposes of the "70/30" rule. The provisions are applicable to sales, exchanges, or distributions after the date of enactment.

16. Affiliated groups

The conference agreement redefines "affiliated group" for all Federal income tax purposes. In general, one corporation will not be affiliated with another unless one owns stock possessing (1) at least 80 percent of the total combined voting stock, and (2) at least 80 percent of the total value of all outstanding stock (disregarding certain preferred stock) of the other. Technical provisions are included, and broad regulatory authority is provided.

The provision is generally effective for taxable years beginning after December 31, 1984. Special and transitional rules are provided.

17. Exchange of stock-for-debt

The conference agreement provides that a corporation transferring stock to satisfy its debt obligations will recognize income to the extent the principal of the debt exceeds the value of the stock. This rule will not apply to insolvent corporations or corporations under title 11. The provision generally applies to transfers after the date of enactment. Certain transitional rules are provided.

E. Partnerships and other Pass-through Entities

1. Allocations of partnership income or loss

a. Contributed property

Under present law, a partnership may elect to allocate depreciation, depletion, or gain or loss with respect to contributed property to reflect variations between the basis of the property and its fair market value when contributed. In the absence of the election, it is possible that the gain or loss with respect to contributed property may be effectively shifted among members of the partnership.

Under the conference agreement, the allocation of partnership items to reflect built-in gain or loss with respect to contributed property will be made mandatory. The provision applies to contributions made after March 31, 1984.

b. Partnership losses

Under present law, retroactive allocation of partnership deductions to partners entering late in the year is prohibited. Nonetheless, it may be possible to accomplish such an allocation through the use of tiered partnerships or, in the case of cash method partnerships, by delaying actual payment for accrued expenses.

With respect to the tiered partnership technique, the conference agreement generally requires items of income, gain, loss, deduction and credit passing from a subsidiary partnership to a parent partnership to be allocated equally among the days in the parent's taxable year for which it has an interest in the subsidiary. Further, for cash basis partnerships, certain items such as taxes, interest, and rents are to be allocated proportionately over the periods to which they relate, so that a partner generally can be allocated only those items actually accrued while he is a partner. The provision applies to items paid or accrued after March 31, 1984.

2. Conversion or deferral of income

a. Disguised payments

Under present law, amounts expended to organize or promote a partnership generally must be capitalized. Other payments for property or services may also be required to be capitalized. It has been suggested that these capitalization requirements may, in effect, be avoided when the payee is also a partner by allocating a greater share of income to that partner.

The conference agreement provides that when a partner performs services for, or transfers property to, a partnership and receives a related allocation and distribution of partnership income or gain, the allocation and distribution, if properly so characterized, will be treated as a transaction occurring between the partnership and a person who is not a partner. The provision applies to services performed or property transferred after February 29, 1984.

b. Disguised sales

Under present law, a partner may be able to avoid recognition of gain on the sale of property to a partnership or another partner by characterizing the transaction as a contribution of the property followed by a distribution of cash or other property to the contributing partner.

The conference agreement provides that, when properly so characterized, a transfer of property to a partnership and a related transfer to that or another partner will be treated as a sale between partners or between the partnership and one who is not a partner. The provision generally applies to transfers after March 31, 1984 subject to certain transitional rules.

c. Gain or loss on contributed property

Present law provides that if certain ordinary income property of a partnership is distributed to a partner, its character as ordinary income property is preserved in the hands of the distributee for at least five years. No comparable rule applies to property contributed to a partnership. Thus, it may be possible to change the character of property from ordinary income to capital gain or from capital loss to ordinary loss through a contribution to a partnership.

Under the conference agreement, the ordinary income or loss character of unrealized receivables contributed to a partnership will be preserved in the hands of the partnership. Further, the ordinary income or loss character of inventory items will be preserved in the hands of the partnership for five years. Built-in losses on capital assets contributed to a partnership are treated as capital losses if recognized by the partnership within 5 years. The provision applies with respect to property contributed after March 31, 1984.

d. Ordinary income property in tiered partnerships

Under present law, amounts received by a transferor partner in exchange for all or part of his partnership interest that are attributable to his interest in ordinary income assets of the partnership are treated as ordinary income. It has been argued that this rule can be avoided if ordinary income assets are held in lower-tier partnership and an interest in the upper-tier partnership is sold, exchanged or distributed.

The conference agreement treats a partnership that owns an interest in another partnership as owning its proportionate share of the ordinary income assets of such partnership directly. A similar rule applies to interests in trusts. The provision applies to distributions, sales or exchanges after March 31, 1984.

3. Transfers of partnership and trust interests by corporations

Under present law, when a partnership interest is sold, any gain is ordinary income to the extent attributable to certain ordinary income items of the partnership. When a corporation distributes property, or sells property in the course of certain complete liquidations, recapture income is taxed to the corporation while non-recapture gain attributable to appreciation in the transferred property goes unrecognized. It has been argued that the corporate recapture provisions do not apply to the distribution or liquidating sale of an interest in a partnership that holds recapture property.

Under the conference agreement, a corporate distribution or a liquidating sale of a partnership interest is treated as a transfer of the distributing corporation's proportionate share of certain recapture items (and other corporate recognition property) held by the partnership. The provision also clarifies that a distribution is treated as a sale or exchange for purposes of the basis adjustment rules. The provision applies to distributions after March 31, 1984.

4. Like-kind exchanges of partnership interests: deferred like-kind exchanges

Under present law, like-kind exchanges of property held for productive use or investment are permitted to be made tax-free. These rules do not apply to inventory, stock, certificates of trust or beneficial interests, or other securities or evidences of indebtedness. In some cases, the courts have permitted tax-free like-kind exchanges of partnership interests. The Treasury has not acquiesced in these holdings. The conference agreement provides that tax-free like-kind exchange treatment is not available for exchanges of interests in different partnerships that are subject to tax under the partnership rules of the Code. If a partnership has elected out of partnership taxation, the exchanges of interests will be treated as exchanges of the underlying assets. The provision applies (subject to certain transitional rules) with respect to transfers after the date of enactment.

Under present law, an intended like-kind exchange transaction may be held open for as long as five years under the case law. The conference agreement provides that property which is received in an exchange and is either not designated within 45 days of the time that the taxpayer transfers his property or received more than 180 days after the taxpayer transfers the relinquished property (or, if earlier, after the due date of the taxpayer's return), will not be treated as like-kind property. This provision generally will apply to transfers of property made after the date of enactment.

5. Use of partnerships to step-up basis

Under present law, a partnership can elect to increase the basis of its assets by the amount of any basis that is "lost" when a distributee partner's basis in his interest is substituted for the basis of distributed property. Thus, a partnership distributing high basis property to a low basis partner will experience an increase in the basis of its other property, but the distributee partner will lose basis and be exposed to greater gain if the distributed property is sold. This result can be avoided be contributing the high basis property to a lower tier partnership which has not elected to make basis adjustments, and by distributing the partnership interest to the low basis partner. The result is that the partnership property of the first partnership will experience a basis increase without reducing the basis of the property.

The conference agreement eliminates the elective basis adjustment for distributions of interests in partnerships that have not elected to make basis adjustments. The provision applies to distributions after March 1, 1984.

6. Allocation of liabilities to partners

The conference agreement reverses the holding of *Raphan* v. *United States* (U.S. Claims Court No. 952-78, September 26, 1983), and instructs the Treasury to amend its regulations relating to the treatment of liabilities of partners and partnerships for purposes of section 752.

F. Trust Provisions

1. *Multiple trusts*

Treasury regulations prevent grantors of trusts from reducing present taxation by establishing multiple trusts for the same beneficiaries to take advantage of the separate graduated rates applicable to each trust. A recent court decision held these regulations to be invalid. Under the conference agreement, trusts established by substantially the same grantors for substantially the same beneficiaries with a principal purpose of tax avoidance will be consolidated for tax purposes under Treasury regulations. The provision is generally effective for taxable years beginning after March 1, 1984.

2. *Trust distributions*

Under present law, beneficiaries are taxed on amounts distributed from a trust (or estate) to the extent of the trust's (or estate's) distributable net income. The trust (or estate) is allowed a deduction for amounts taxed to its beneficiaries. Distributions of appreciated property are deemed to carry out distributable net income to the extent of the property's value at the time of distribution. The basis of the property in the hands of the beneficiary is its value to the extent it carries out distributable net income.

Under the conference agreement, distributions of property are treated as carrying out distributable net income only to the extent of the property's basis. The beneficiary's basis will be the same as the trust's (or estate's) and the appreciation no longer will be exempted from tax. Alternatively, the trustee or executor may elect to recognize gain at the the trust level upon distribution of such property.

The provision applies to distributions after June 1, 1984.

G. Time Value of Money and Other Accounting Provisions

1. Deferred payment transactions

a. Time for inclusion or deduction of deferred interest

Present law provides that, in general, in a discount lending transaction, the borrower is treated as having paid, and the lender as having received, the annual unpaid interest, which is then relent to the borrower. These original issue discount (OID) rules match the interest inclusion by the lender with the interest deduction by the borrower. The OID rules of present law do not apply to obligations issued in exchange for property where neither the obligation nor the property is publicly traded; to obligations issued by individuals; or, as to holders of discount obligations, to obligations not held as capital assets.

The conference agreement extends the OID rules to obligations issued for nontraded property, issued by individuals, and not held as capital assets. The interest element in obligations issued for nontraded property is to be compared to a test rate. The test (safe harbor) rate is 110 percent of an average yield on Federal obligations of similar maturity (the "applicable Federal rate"). This yield is to be redetermined semi-annually for 3 categories of maturities (short-, medium-, and long-term). If interest is not stated at least at the safe harbor rate, interest will be imputed at a rate equal to 120 percent of the applicable Federal rate and annually included in the income of the lender and deducted by the borrower at that rate. If interest is stated at or above the safe harbor rate but is paid annually at less than that rate, interest will be accrued annually by the lender and borrower at the stated rate. Exceptions to these rules are provided for sales of principal residences, certain sales of farms, sales involving total payments of $250,000 or less, and issuers of obligations issued in a sale of assets not used by the purchaser in a trade or business or held by the purchaser for investment.

The conference agreement also provides exceptions to the OID rules for loans of $10,000 or less between individuals, purchases of assets that do not constitute trade or business or investment assets in the hands of the purchaser, and for borrowers in negative amortization loan transactions where the loan proceeds are used to purchase non-business or non-investment property. These provisions generally apply to transactions entered into after December 31, 1984, except for sales or exchanges with respect to which there was a binding commitment on March 15, 1984.

b. *Measurement of interest in deferred payment transactions*

Under present law, if the parties to a deferred payment sale fail to state interest at a safe-harbor rate fixed by regulation, interest is imputed at a higher rate fixed by regulation. The safe-harbor rate is a simple interest rate; the imputed rate is a compound rate. Imputed interest is allocated among deferred payments in proportion to the amount of the payment, without regard to the period of time that has elapsed since the sale.

The conference agreement provides that the adequacy of the interest element in a deferred payment sale is to be tested against a self-adjusting compound rate of interest which approximates a market rate. This test (safe-harbor) rate is the same rate applied under the proposed amendments to the OID rules: 110 percent of the applicable Federal rate. If insufficient interest is stated, interest is to be imputed at a rate equal to 120 percent of the applicable Federal rate. Interest income will be recognized by the lender and interest expense will be deducted by the borrower on an economic accrual basis when paid (in the case of a cash method taxpayer) or when due (in the case of an accrual method taxpayer). An exception is provided for purchasers of assets that do not constitute trade or business or investment assets in the hands of the purchaser.

In the case of certain sales of principal residences and farm land subject to the deferred payment rules of section 483 rather than the OID rules (i.e., sales of personal residences and the sale of a farm by an individual or small business where the total payment is less than $1,000,000) the test and imputed interest rates of section 483 will be fixed by the procedures provided by present law (i.e., adjusted from time to time as appropriate by the Treasury in regulations). In the case of sales of personal residences where the sale price is less than $250,000 the rates set in Treasury regulations will apply. To the extent the sales price exceeds $250,000, the rates computed with reference to the applicable Federal rate will apply. The maximum amount of deferred payments that is subject to the rate set by Treasury regulations is $250,000. This amount is reduced on a sliding scale as the selling price rises above $250,000. Thus, where the sales price of a personal residence exceeds $250,000, present law rates would apply to that portion of the deferred payments that $250,000 bears to the sales price; the rates computed under the new procedures apply to the remainder. The exceptions provided for personal residences and farms only apply to the test and imputed rates; even where the exceptions apply and the existing procedures to compute the rates are used, the rate will be computed on a compound basis and interest will be allocated among payments as provided under the general rule of the conference agreement.

The conference agreement generally applies to sales or exchanges after December 31, 1984, except for sales or exchanges with respect to which there was a binding commitment on March 15, 1984. However, as to any transactions entered into after June 8, 1984, and before January 1, 1985, the conference agreement provides that a deduction will not be allowed for interest in excess of the amount properly allocable to the period.

2. Deferred payments for use of property and services

Under present law, a lessor of property reporting income on the cash method includes rents from the property in income in the year in which the rent is actually or constructively received; an accrual method lessor reports rental income in the year in which all events fixing the lessee's liability for the rent have occurred and the amount thereof can be determined with reasonable accuracy (the "all-events test"). A cash method lessee otherwise entitled to deduct rent generally claims a deduction in the year the rent is paid; an accrual method lessee generally deducts rent in the year the all-events test is satisfied. An accrual basis lessor or lessee which is a party to a lease under which rents are not payable currently normally accrues a ratable portion of the rent income or expense in each year of the lease.

The conference agreement requires that rental and interest income attributable to a deferred rental payment agreement be reported as income by the lessor and deducted by the lessee as if both were on the accrual method, irrespective of their actual methods of accounting. If a transaction is subject to these provisions, the amount of rent to be accrued by the parties for a taxable year will be based upon a rental rate that is stated in the lease for each period of the lease.

In the case of long-term leases and sale-leaseback transactions, where rents are stepped and the reason for the stepping of the rents is tax avoidance, then the amount of rent will be based upon a rental rate that is constant or level for each period of the lease. For this purpose, a lease is a long-term lease if its length is greater than 75 percent of the ACRS life (i.e., 13.5 years in the case of real property).

In addition, in the case where payment of rent is deferred beyond the end of the calendar year subsequent to the year to which the rent relates and where rents are treated as level rents, the lessor will annually accrue interest income, and the lessee will deduct interest expense, at a rate equal to 110 percent of a self-adjusting statutory rate, on any unpaid accrued rent and interest.

Deferred payments under service contracts are treated in a manner similar to deferred rents, except that the annual inclusion and deduction rules apply only to the imputed interest element of the transaction.

Exceptions are provided for deferred payment transactions involving total payments of $250,000 or less and certain other situations.

The provisions are effective for agreements entered into after June 8, 1984, for taxable years ending after such date.

3. Premature accruals

Under the accrual method of accounting, an expense is deductible when all events have occurred which establish the fact of liability and the amount of the liability can be determined with reasonable accuracy. The proper time for deducting expenses for which economic performance has not yet occurred is the subject of controversy under present law.

The conference agreement generally requires that economic performance must occur before all events establishing the fact of liability will be considered to have occurred. Exceptions are made for items for which specific timing rules are already provided under the Code, such as bad debts and vacation pay. In addition, the conference agreement provides a general exception for ordinary business expenses of a recurring nature that are consistently accounted for by the taxpayer.

The conference agreement permits utility companies owning nuclear power plants to take deductions for contributions to a segregated reserve fund dedicated to plant decommissioning, subject to certain limits. This reserve fund will be taxed as a separate entity, with respect to fund earnings, at the maximum corporate tax rate (46 percent). The conference agreement requires that all customer charges for decommissioning are to be included in the income of the company that is providing the services.

The conference agreement also provides an elective method for deducting site reclamation and closing costs of surface and deep mines and solid, liquid, and hazardous waste disposal sites (not including certain designated superfund sites), associated with meeting the requirements of Federal or State law (and local ordinance or permit in the case of a waste disposal site).

The conference agreement provides a 10-year carryback for losses arising from certain deferred liabilities and a longer period for certain losses associated with the decommissioning of nuclear generating plants (but not to a taxable year beginning before January 1, 1984, unless otherwise permitted by present law).

The conference agreement applies to expenses accruing after the date of enactment, subject to certain elective transition rules.

4. Prepayment of expenses

Except with respect to interest and prepayments by farm syndicates, present law is unclear as to the proper timing of a deduction for prepaid items by cash method taxpayers. In the case of interest, deductions are allowed only for the year to which the interest relates. A similar rule applies to prepaid expenses of farm syndicates.

Under the conference agreement, tax shelter organizations will not be permitted to deduct any amount prior to the time it would be properly deductible under the accrual method of accounting (or under section 464 in the case of farming tax shelters). The conference agreement defines tax shelter organizations to include certain partnerships and enterprises, and any entity, plan or arrangement having the principal purpose of tax avoidance.

An exception is provided under which prepaid expenses are deductible under the rules of present law if economic performance with respect to an item occurs before the 90th day after the end of the taxable year. For the purpose of this exception only, in the case of oil and gas activities, economic performance is deemed to occur when commencement of the well begins (i.e., the well is "spudded"). The amount of prepaid items which may be deducted under this exception is limited to the cash investment by the taxpayer in the tax shelter.

These rules apply to prepayments made after March 31, 1984.

5. Construction period interest and taxes for residential property

Under present law, taxpayers are generally required to capitalize construction period interest and taxes on real property other than low income housing. This rule does not apply to residential real property acquired, constructed or carried by a corporation (other than an S corporation).

The conference agreement requires corporations to capitalize construction period interest and taxes for residential real property other than low income residential real property. This change will apply to interest and taxes paid or incurred in taxable years beginning after December 31, 1984, for construction of residential real property begun after March 15, 1984.

6. Pre-opening expenditures

Under present law, taxpayers may elect to amortize pre-opening or start-up expenditures over the first five years after the business is opened. If the election to amortize is not made, the IRS views these expenditures as nondeductible capital items. Certain taxpayers, nevertheless, claim those items as currently deductible if the five-year amortization election is not made.

The conference agreement provides that pre-opening or start-up expenditures (other than interest, taxes, and research and experimental expenses) must be amortized over a five-year period. The provision is effective for taxable years beginning after June 30, 1984.

H. Straddles and Other Securities Transactions

Under present law, several special rules apply to limit tax benefits from straddle transactions. Under the loss deferral rule, losses on straddles are deferred to the extent of gains on offsetting positions. However, there is an exception from this rule for straddles involving stock and stock options. Also, a mark-to-market system applies to regulated futures contracts under which taxes are paid on unrecognized gains and losses at the end of each year. Under the mark-to-market rules, gains and losses are treated as 60-percent long-term and 40-percent short-term, providing a maximum tax rate of 32 percent. The tax treatment of options on futures contracts and cash settlement options is unclear under present law.

The conference agreement repeals the exception from the loss deferral rule for stock options and stock offset by an option or by a position other than stock in substantially similar or related property (as determined under regulations), and substitutes a limited exception applying to covered calls which are not deep-in-the-money. The exception from the straddle rules for stock will not apply where the corporation is formed or availed of to enter into positions to offset the shareholder's own positions. When a taxpayer has written an in-the-money call that is not deep-in-the-money, the conference agreement requires long-term treatment for any loss on the call if gain on the stock would be long-term and excludes from the holding period applicable to the stock any period during which the taxpayer is the grantor of such an option. The conference agreement also subjects certain year-end losses from such options to deferral where the stock is disposed of soon after the option is closed but gain from the stock is in a later year.

The conference agreement also extends the mark-to-market system to options (other than stock options and certain narrow-based stock index options) and to options held by options market makers.

The conference agreement modifies the hedging exception to the anti-straddle rules to reduce the possibility that it may be used to generate losses that shelter unrelated income from tax.

The Treasury Department's authority to issue regulations with regard to the straddles rules is extended so that it can deal with the problems presented under present law by mixed straddles. The conference agreement requires the regulations to provide rules that permit offsetting of gains and losses in mixed straddles by identification of each mixed straddle or by establishment of a mixed straddle account. The regulations are also to provide rules dealing with the requirement that carrying costs of a straddle position be capitalized. Treasury's authority to prescribe effective identification requirements for the hedging exception and broker-dealer investment accounts is also broadened.

The wash-sale rule is extended to apply to short sales, including short sales "against the box." The present exception from the wash-sale rule is limited to dealers in stocks and securities effective after December 31, 1984.

The conference agreement clarifies the treatment of cash settlement options and options on futures contracts.

The repeal of the exception for stock options from the anti-straddle rules is effective for positions entered into after December 31, 1983. The extension of mark-to-market rules is effective for positions entered into after the date of enactment. Transition rules are provided similar to those which were provided when the mark-to-market system for regulated futures contracts was implemented in 1981.

The conference agreement clarifies that straddle losses prior to 1982 are to be allowed in certain cases where they were incurred in a transaction entered into for profit.

I. Foreign Provisions

1. Maintaining the source of U.S source income

Under present law, the United States taxes the U.S. source income of U.S. taxpayers. U.S. taxpayers' foreign source income can be free of U.S. tax under the foreign tax credit. U.S. taxpayers can place the "foreign" label on some U.S. source income (such as interest and insurance premiums) by routing it through a foreign corporation. Interest and dividend payments from, and income inclusions on account of, this foreign corporation are foreign source income to their U.S. owners. This newly-created foreign source income may escape U.S. (and foreign) tax.

The conference agreement prevents re-labelling of U.S. source income as foreign source income. Under the conference agreement, subpart F and foreign personal holding company inclusions are U.S. source income to the extent attributable to U.S. source income of the foreign corporation with respect to which the inclusions are required. If a foreign corporation has earnings and profits and 10 percent or more of the earnings and profits are attributable to U.S. sources, then (1) interest paid by the foreign corporation to its 10-percent U.S. shareholder (or a related person) is U.S. source income to the extent properly allocable to U.S. source income of the foreign corporation, and (2) a pro rata portion of dividends paid by the foreign corporation out of the earnings and profits is U.S. source income. The conference agreement applies only to 50-percent U.S-owned foreign corporations. Generally, it applies with respect to income earned by paying corporations after the date of enactment. Transitional rules are provided. The foreign tax credit limitation generally will be computed separately for income that benefits from the transitional rules.

2. Maintaining the character of interest income

Under present law, a U.S. taxpayer's foreign interest income cannot escape both U.S. and foreign tax (under the United States' separate foreign tax credit limitation that prevents foreign taxes on noninterest income from offsetting U.S. tax on foreign interest income). U.S. taxpayers can circumvent this rule by having foreign subsidiaries earn foreign interest income (for example, by depositing money in foreign banks). When the U.S. taxpayer is taxable on the earnings of its foreign subsidiary, its income is not separate limitation interest income. Thus, newly recharacterized "non-interest" income may totally escape both U.S. and foreign tax.

The conference agreement generally subjects to the separate foreign tax credit limitation for interest the following: subpart F and foreign personal holding company inclusions of, and dividends and interest received by, a U.S. person that attributable to separate limitation interest income of a 10-percent U.S.-owned foreign corporation or a RIC. Inclusions and payments are treated as separate limitation interest to the extent of the separate limitation interest income of the foreign corporation or RIC. The provision applies only if the foreign corporation or RIC has earnings and profits for the taxable year to which the inclusion or payment is attributable and 10 percent or more of the earnings and profits is attributable to separate limitation interest. Interest payments to 10-percent U.S. shareholders (or related persons) do not reduce separate limitation interest or earnings and profits of the paying corporation for these purposes. The provision generally applies to income earned by paying corporations in taxable years beginning after the date of enactment. However, interest income earned with respect to investments by a taxpayer after June 22, 1984 (the date of conference action) will be treated as separate limitation interest. Transitional rules are provided.

3. Factoring trade receivables

Under present law, a seller who sells goods for the buyer's receivable (a transferable debt) may sell that receivable to a third party—a factor—at a discount. If a U.S.-owned factor is in a tax haven, it may earn income free of U.S. tax. That income may be eligible for deferral, and it may be foreign source income that is sheltered by excess foreign tax credits. Further, when a foreign subsidiary of a U.S. corporation invests in U.S. property, that investment is taxable as a dividend to the U.S. parent. Some taxpayers allege that this rule does not apply to a foreign factoring subsidiary that buys receivables from its U.S. parent.

Under the conference agreement, when a foreign factoring subsidiary of a U.S. owner gets cash for a receivable that (1) it bought from a related person, and (2) the related person had taken in exchange for services or inventory, the U.S. owner is taxed on that factoring income. The conference agreement treats a purchase of receivables like a loan to the purchaser of the goods or services with all income attributable to receivables (and income from financing export transactions) treated as interest subject to the separate foreign tax credit limitation. The conference agreement also treats payments of cash from a foreign subsidiary to a related U.S. person for receivables arising from the U.S. person's sales of services or inventory as investments in U.S. property if the purchaser of the services or goods is a U.S. person. Thus, payments of cash for these receivables will be taxable as dividends to the U.S. parent, whatever the term of the obligation under the receivable. This provision will generally apply to accounts receivable and evidences of indebtedness transferred after March 1, 1984 in taxable years ending after that date.

4. Source of transportation income

Under present law, in general, the United States taxes all U.S. income, but not always all foreign income, of United States persons. In general, the United States does not tax the foreign income of foreign persons (such as foreign corporations). Under present law, transportation income can be almost all foreign even if the transportation is between two U.S. points, if the route of transport lies primarily outside the United States' three mile territorial limit.

Under the conference agreement, transportation income earned from transportation that begins and ends in the United States is treated as U.S. income. Transportation income earned from transportation that begins in the United States and ends in a U.S. possession (or vice-versa) is treated as 50-percent U.S. source income, except in the case of certain income earned from aircraft leasing. Income earned from transportation includes services income and leasing income from ships, airplanes, and containers used in connection with ships and airplanes. The effective date is the date of enactment.

5. Foreign investment companies

Under present law, taxpayers contend that a foreign corporation that is widely held by U.S. persons may establish a subsidiary to invest in U.S. commodities markets without any of the parties incurring U.S. tax. They also contend that when the U.S. shareholders eventually dispose of their shares in the foreign corporation they will be subject to tax at only the capital gains rate.

The conference agreement will, in certain cases, apply the accumulated earnings tax to earnings from U.S. investments, even after those earnings pass through corporate solution as dividends or interest. This provision applies generally to distributions received on or after May 23, 1983. It will also generally treat gains of U.S. shareholders from those investments as ordinary income. This provision applies generally to sales or exchanges on or after September 29, 1983.

6. Extension of moratorium on application of research and experimental expense allocation regulation

In determining foreign source taxable income for purposes of computing the foreign tax credit limitation, taxpayers must allocate or apportion expenses between foreign source income and U.S. source income (Code secs. 861-863). Rules for allocating and apportioning research and other expenses are set forth in Treasury Regulation sec. 1.861-8.

In the Economic Recovery Tax Act of 1981 (ERTA), Congress directed the Treasury Department to study the impact of its section 861 regulations on research activities conducted in the United States and on the availability of the foreign tax credit. Congress also provided that for a taxpayer's first two taxable years beginning after the date of enactment of ERTA (August 13, 1981), all research expenditures in those years for research activities conducted in the United States are to be allocated or apportioned to sources within the United States. This two-year moratorium on the application of the research and experimental expense allocation rules of Treas. Reg. sec. 1.861-8 does not apply to subsequent taxable years.

The conference agreement generally extends for two more years the moratorium on the application of the Treasury research expense allocation rules. The extension generally applies to a taxpayer's taxable years beginning after August 13, 1983 and on or before August 1, 1985.

The conferees expect the Treasury Department to utilize the extension period to determine finally whether the allocation of all U.S.-based research expenditures to U.S. sources is an effective research incentive compared to other possible research incentives.

The conferees expect and hope that further extensions will be unnecessary.

The extension applies only to the allocation of research expenses for the purpose of geographic sourcing of income. It does not apply for other purposes, such as the computation of combined taxable income of a DISC (or FSC) and its related supplier.

7. Repeal of 30-percent tax on portfolio interest paid to foreign persons

Payments of passive income (interest, dividends, royalties, etc.) to foreign persons generally are subject to a 30-percent U.S. withholding tax if the payments are not effectively connected with a U.S. trade or business conducted by the foreign person. Exemptions from the tax are provided in certain situations. Some U.S. tax treaties reduce the tax. In the case of interest, some treaties eliminate the tax.

The Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) generally requires registration of debt obligations. An exemption from the registration requirement is provided for debt obligations that are sold under procedures reasonably designed to prevent sale or resale to U.S. persons, that bear interest payable outside the United States only, and that indicate that U.S. holders are subject to tax penalties.

The conference agreement generally repeals the 30-percent withholding tax on interest paid on portfolio indebtedness by U.S. borrowers to nonresident alien individuals and foreign corporations. The repeal generally is effective for interest paid on a portfolio obligation issued after the date of enactment, provided the obligation, if in bearer form, is excluded from the TEFRA registration requirement under the exemption described above or, if in registered form, is certified to be held by a foreign person.

Otherwise eligible interest paid to a controlled foreign corporation (unless paid by a related party) will be exempt from the 30-percent tax, but will be subject to the subpart F rules without regard to the usual exceptions. Interest paid to banks and 10-percent or greater owners of the payor will not be exempt from the 30-percent tax.

The conference agreement grants the Secretary of the Treasury discretion to require registration of obligations excluded from the TEFRA registration requirement under the exemption described above. It also provides that interest paid to certain controlled foreign corporations will be treated as paid to a resident of the country in which the controlled foreign corporation is incorporated, if certain requirements are met.

8. Foreign investors—original issue discount and coupon stripping

Foreign investors acquiring pure original issue discount corporate bonds—those with no payment of interest until maturity—defer U.S. taxation until they surrender the bonds at maturity. The rules governing timing of income inclusion for foreign investors holding corporate OID debt differ in some respects from those governing income inclusion for U.S. investors. As for foreign holders of debt originally issued at a discount by obligors other than corporations and governmental entities, existing law is unclear.

The conference agreement conforms the timing of income inclusions for foreign investors to the timing for comparable U.S. investors, except that there is no inclusion for foreign investors until actual receipt of payment. The conference agreement also conforms the treatment of noncorporate debt to the treatment of corporate debt. These provisions generally apply to payments made on or after the 60th day after the date of enactment. The agreement denies a deduction to a U.S. borrower that accrues interest on original issue discount debt to a related foreign lender until payment of the interest. This provision is effective for obligations issued after June 9, 1984.

The Internal Revenue Code does not contain specific rules governing foreign investors who sell or surrender stripped bonds or who sell stripped coupons. The conference agreement generally conforms the rules governing foreign investors to those governing U.S. investors, except that there is no inclusion for foreign investors until actual receipt of payment. Thus, foreign investors will treat stripped coupons and stripped bonds as being OID instruments. These provisions will apply generally to payments made on or after the 60th day after enactment.

9. Withholding on dispositions by foreigners of United States real property interests

Under the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA), foreign persons who dispose of U.S. real property interests generally are required to pay tax on any gain realized on the disposition. FIRPTA provides for enforcement of the tax on foreign persons through a system of information reporting designed to identify foreign owners of U.S. real property interests.

The conference agreement generally imposes a withholding obligation when a U.S. real property interest is acquired from a foreign person. The withholding duty generally applies to purchasers of U.S. real property interests from foreign owners unless they receive a sworn affidavit stating that the seller is not foreign and containing the seller's taxpayer identification number ("nonforeign affidavit"). The IRS may require the purchaser to file the nonforeign affidavit with it to obtain this exemption from withholding. If the purchaser has actual knowledge or has received formal notice that the nonforeign affidavit is false, the affidavit will not override his withholding duty. Agents for transferors and transferees are liable for withholding if they have actual knowledge that a nonforeign affidavit is false and fail to notify the transferee. This withholding duty is limited to the agent's compensation. In the case of a foreign corporate transferor, an agent of the transferor will be deemed to have actual knowledge that any nonforeign affidavit is false.

Special rules are provided for withholding by partnerships, trustees, executors, and certain distributing foreign corporations and domestic U.S. real property holding corporations.

Withholding does not apply to a purchaser buying U.S. real property for $300,000 or less, for use as his residence, or to the sale of stock that is regularly traded on an established securities market. Withholding does not apply if the purchaser receives a qualifying statement that the seller is exempt from tax, security has been provided, or other arrangements for payment of tax have been made. Withholding generally does not apply to a sale of stock in a nonpublicly traded U.S. corporation if the purchaser receives a sworn statement that the corporation is not a U.S. real property holding corporation. The IRS may require the purchaser to file this statement with the IRS to obtain this exemption from withholding. If the purchaser has actual knowledge or had received formal notice that the statement is false, withholding is required.

The amount withheld generally is the lesser of 10 percent of the price, or the maximum tax liability on disposition (after proof of basis). A refund of any amounts withheld in excess of the maximum tax liability may be requested before a tax return would otherwise be filed. The IRS can also reduce or eliminate withholding on request in certain other cases.

The conference agreement generally repeals the information requirements of FIRPTA. However, the Secretary may require reporting by foreign persons not engaged in a U.S. business who hold direct investments in U.S real property of $50,000 or more.

Withholding will apply to dispositions on or after January 1, 1985. The changes in the reporting requirements are effective retroactively to calendar year 1980.

10. Use of territories to avoid U.S. tax on foreign investors

Under present law, payments of U.S. source interest, dividends, and other passive income to foreign investors are generally subject to a 30-percent U.S. withholding tax. The United States does not tax payments of passive income to corporations organized in Guam, the Northern Mariana Island, or the U.S. Virgin Islands. Some argue that foreigners who wish to invest in the United States may avoid both U.S. and territorial tax by channeling their investments through conduit corporations in these territories.

Temporary Treasury regulations subject dividends and interest paid by territorial conduit corporations to territorial withholding tax. Guam is contesting these regulations in court.

Under the conference agreement, interest, dividends, and other passive income paid from U.S. sources to corporations organized in Guam, the Marianas, or the Virgin Islands are subject to U.S. tax unless the bulk of the recipient's gross income is from territories and unless the bulk of its beneficial owners are local residents. The provision applies with respect to payments made after March 1, 1984.

11. Taxation of certain transfers of appreciated property outside the United States

Under present law, certain transfers of appreciated assets to foreign corporations in reorganizations and liquidations, which would be tax-free, are taxable if the Internal Revenue Service rules that one of the principal purposes of the transfers was the avoidance of Federal income tax. Under Internal Revenue Service guidelines, generally, transfers of property used in the active conduct of a foreign trade or business are not taxed. However, also under those guidelines, transfers of assets containing built-in gain (such as inventory and accounts receivable) are generally taxed.

Judicial interpretation of the principal purpose test has reduced the ability of the Internal Revenue Service to administer these rules. In addition, the Internal Revenue Service's current ruling policy permits the tax-free transfer of intangible property abroad, where the development of the property generated significant U.S. tax benefits but the income derived from the property may escape U.S. taxation. Finally, the courts have rejected the Internal Revenue Service's requirement that certain losses be recaptured upon the incorporation of a foreign branch by a U.S. person.

Under the conference agreement, the rules governing transfers of appreciated property abroad are amended to provide for gain recognition without regard to purpose, unless the property is transferred for use in an active trade or business abroad. Certain transfers of assets containing built-in gain are automatically subject to tax. Transfers of stock are subject to the active trade or business test. In addition, transfers of intangibles that would otherwise be tax-free are subject to tax. The intangibles rule does not apply to good will or going concern value developed by a foreign branch.

To the extent provided in regulations, a domestic corporation will recognize gain on liquidating distributions of appreciated property to foreign persons; present law in this area will continue to apply until regulations are promulgated.

The current Internal Revenue Service policy on incorporations of foreign branches generally is codified. Gain recognized on such incorporations will not exceed previous net losses of the foreign branch and will have the character of the previous losses. In the case of a previous overall foreign loss, the amount of gain recognized will be reduced by the amount recognized under Code section 904(f)(3) in the loss year, but not amounts simply recharacterized as U.S. source income by Code section 904(f)(1).

The provision generally applies to transfers after January 1, 1985. A transitional rule is provided for ruling requests filed before March 1, 1984. Transfers of intangibles that occur after June 6, 1984 (the date of conference action) and before January 1, 1985 will be presumed to have a tax avoidance purpose, subject to terms and conditions prescribed by the Secretary.

12. Provisions relating to foreign personal holding companies

The conference agreement clarifies the family and partner attribution rules for determining when a foreign corporation is a foreign personal holding company. It also prevents avoidance of U.S. tax by interposition of a foreign trust or other foreign entity between a foreign personal holding company and a U.S. taxpayer. In addition, the conference agreement coordinates the foreign personal holding company rules with the controlled foreign corporation rules. It provides that shareholders of a controlled foreign corporation (that is also a foreign personal holding company) are subject to the controlled foreign corporation rules to the extent that income taxable under those rules exceeds income taxable under the foreign personal holding company rules. These provisions generally apply to taxable years beginning after the date of enactment. The agreement also extends the same country dividend exception of subpart F to the foreign personal holding company rules. This provision applies to taxable years beginning after March 15, 1984.

13. Decontrol of foreign corporations

Under present law, when a U.S. taxpayer who is a 10-percent shareholder of a controlled foreign corporation sells or exchanges stock in a taxable transaction, the gain is treated as ordinary (dividend) income to the extent of the shareholder's pro rata share of the corporation's post-1962 accumulated earnings and profits. A U.S. corporation that disposes of stock by distributing it as a dividend-in-kind or in the course of liquidation, in a transaction otherwise eligible for nonrecognition treatment to the U.S. corporation, is also required to include in income its share of post-1962 accumulated earnings and profits. Taxpayers have taken the position that this rule does not apply if a controlled foreign corporation that is wholly owned by a U.S. corporation issues new shares for shares of the U.S. corporation. If this position were sustained, such a transaction could lead to permanent exemption from U.S. corporate tax of the earnings of the controlled foreign corporation accumulated prior to the exchange.

Under the conference agreement, certain exchanges by a controlled foreign corporation of its newly issued stock for shares of its U.S. parent corporation are treated as sales or exchanges by the U.S. parent of stock in the controlled foreign corporation. The conference agreement also clarifies the rules that tax the previously untaxed earnings and profits of a controlled foreign corporation at ordinary income rates when its U.S. owner disposes of the shares or liquidates the corporation. It prevents later double taxation of those earnings and profits and double crediting of associated foreign taxes. It also treats direct ownership of a controlled foreign corporation like indirect ownership for the purpose of these rules. The provision generally applies as of the date of enactment.

14. Foreign collapsible corporations

Under present law, sales of inventory yield ordinary income, not capital gain. "Collapsible" corporations' assets generally include inventory. Generally, a shareholder's gain on the sale or liquidation of a collapsible corporation is ordinary income rather than capital gain. However, if a collapsible corporation consents under section 341(f) to recognize ordinary income on the disposition of its inventory and the like, the shareholder gets capital gain treatment on the sale or liquidation of the corporation. In the case of a consenting foreign corporation, enforcement of the consent may be impractical.

Under the conference agreement, in general, a section 341(f) consent given by a foreign corporation is not given effect unless regulations provide otherwise. Specifically, this provision is effective for sales or exchanges after the date of enactment.

15. Stapled stock; stapled entities

The conference agreement contains provisions regarding so-called stapled stock. It provides generally that if a foreign and a domestic corporation are stapled entities, the foreign corporation generally will be treated as domestic. In addition, if two domestic corporations are stapled entities, each will be treated as owning the other. This provision is generally effective on the date of enactment.

16. Insurance of related parties by a controlled foreign corporation

Under present law, income that a controlled foreign corporation earns from insuring U.S. risks is currently taxable to its U.S. shareholders; income earned from insuring non-U.S. risks of a related party may not be currently taxable. The conference agreement provides that, for purposes of determining foreign base company services income (which is also currently taxable to U.S. shareholders of a controlled foreign corporation), any services performed with respect to any policy of insurance or reinsurance covering risks of a related party will be treated as having been performed in the country in which the insured risk is located. The result of this provision is that the income from this kind of service will be currently taxable. This provision will apply to taxable years of foreign corporations beginning after the date of enactment.

17. Resident aliens

The conference agreement provides standards for determining whether an alien individual is a resident of the United States. Under these standards, an individual who spends substantial time in the United States in any year or over a three-year period will generally be a U.S. resident. A permanent resident for immigration purposes also will be a U.S. resident. This provision is generally effective on January 1, 1985.

18. Community income of nonresident aliens

Present law allows married couples composed of nonresident aliens to split income for U.S. tax purposes if their home county uses the community property system, but not if it uses the common law system. The conference agreement prevents married nonresident aliens from using the community property laws of their home country to split certain income for U.S. tax purposes. This provision is generally effective on January 1, 1985.

19. Foreign sales corporations

Present law provides a system of tax deferral for Domestic International Sales Corporations (DISCs) and their shareholders. A DISC is a domestic subsidiary of a U.S. company engaged in exporting. The income attributable to exports may be apportioned between the parent and the DISC using special pricing rules.

The conference agreement provides for the establishment of foreign sales corporations (FSCs) which typically will be foreign incorporated subsidiaries of U.S. parent corporations engaged in exporting. To qualify as a FSC, a corporation will have to be organized under the laws of a jurisdiction outside the U.S. customs area and meet certain foreign presence requirements.

The provisions of the conference agreement will apply to the export income of a FSC if it is managed outside the United States and if some economic processes of the transaction take place outside the United States. In addition, the provisions will apply to the export income of a small FSC attributable to up to $5,000,000 of export receipts whether or not its management or economic processes are foreign.

Under the optional administrative pricing rules, a FSC may earn the greater of 23 percent of the combined taxable income that it and a related party derive from an export transaction, or 1.83 percent of the gross receipts from the transaction.

The conference agreement will exempt a portion of the export income of a FSC from U.S. tax. If a transaction is subject to one of the administrative transfer pricing rules, the exempt portion will be 16/23 of the FSC's income from the transaction, generally 16 percent of combined taxable income or 1.27 percent of the gross receipts from the transaction. Under the section 482 pricing rules, the exempt portion is limited to 32 percent of FSC income. The provision of the conference agreement that decreases the benefits for certain corporate tax preference items reduces the exemption by an additional 1/17 for corporate shareholders. The rest of export income will be subject to U.S. tax. Dividends from export income but not investment income paid by a FSC to a U.S. corporate shareholder will be tax-exempt at the corporate shareholder level.

The conference agreement allows U.S. possessions to impose tax on income that arises after January 1, 1987. The conference agreement also clarifies that an FSC organized in a U.S. possession may maintain its office there rather than in a foreign country.

Companies may continue to use the present DISC rules for up to $10 million of export receipts but will be required to pay interest based on the T-bill rate on the deferred tax. In addition, the conference agreement treats actual distributions of accumulated deferred DISC income as having been previously taxed, so that tax on those amounts will be forgiven.

The conference agreement treats deemed distributions for taxable years of DISCs that begin in 1984 and end on December 31, 1984 under the provisions of this conference agreement as occurring over 10 years. Under regulations, taxpayers may elect to accelerate the inclusion income of these deemed distributions.

The conference agreement requires the Treasury Department to undertake a study of the advisability of providing FSC benefits for export services.

This provision generally will apply to transactions after December 31, 1984.

J. Reporting, Penalty, and Other Compliance Provisions

1. Provisions relating to tax shelters

a. Registration of tax shelters and promoter lists

Present law does not provide the Treasury with the means of detecting and tracing tax shelter promotions through the activities of the promoters.

The conference agreement provides for registration of tax shelter promotions with the IRS so that the IRS can more effectively manage its activities with respect to tax shelters. Also, the conference agreement requires promoters to keep a list of their investors for inspection by the IRS.

b. Promoter penalty

The Tax Equity and Fiscal Responsibility Act of 1982 provides for a penalty on promoters and salespersons of abusive tax shelters equal to the greater of $1,000 or 10 percent of gross income to be derived from the activity. The conference agreement increases the 10 percent penalty to 20 percent of gross income. The conference agreement also makes actions aiding and abetting the understatement of tax liability subject to injunction.

c. Interest for tax shelter cases

The conference agreement provides a special, higher interest rate for tax shelter cases of 120 percent of the regular rate, for interest accruing after 1984.

2. Information reporting provisions

a. Mortgage interest reporting

Present law does not require reporting by recipients of amounts (such as mortgage interest) that may be deducted by the payor. The conference agreement provides that persons who, in connection with their trade or business, receive interest payments totaling $600 per year or more on a mortgage must report that interest to the Internal Revenue Service.

b. Cash reporting

Present law provides for reporting of cash transactions by certain financial institutions, but does not require nonfinancial institutions to report receipts of cash.

The conference agreement requires persons who, in connection with their trade or business, receive cash payments from another person in excess of $10,000, to report those payments to the Internal Revenue Service.

c. IRA reporting

Present law generally allows an individual to deduct the amount of qualified individual retirement account (IRA) contributions made for a year, either during the year or before the due date (with extensions) of the income tax return for the year. The conference agreement provides that reports on these contributions are to include the amount and the year to which a contribution relates. The conference agreement also provides that an IRA contribution is not deductible for any year unless made on or before the unextended due date of the return for that year.

d. Foreclosure reporting

Under present law, foreclosures in satisfaction of a debt or forgiveness of a debt may give rise to income to the debtor. The conference agreement requires persons lending in the course of a trade or business to report to the IRS when the security for a loan is acquired by foreclosure or otherwise in satisfaction of all or part of the debt. Reporting is also required when the borrower abandons the security.

e. Disposition of partnership interests

When a partnership interest is sold or exchanged, the transferor partner may have reportable gain or loss under present law. In addition, if the value received is attributable to appreciated inventory or unrealized receivables that could produce ordinary income if sold by the partnership, the transferor will be treated as having realized ordinary income. The conference agreement requires a partnership to inform the Internal Revenue Service, the seller, and the buyer of the fair market value of the allocable share of unrealized receivables and appreciated inventory when partnership interests are sold or exchanged.

f. Reporting on substitute payments

A broker who holds securities for a customer in a street name may lend those securities to another for use in a short-sale. If dividends or interest are paid on the securities before the stock is returned to the broker, the short-seller will make substitute payments to the broker. These payments are not eligible for the dividends received deduction or any otherwise applicable interest exclusion. The conference agreement requires brokers to notify their customers when payments they receive are amounts in lieu of dividends or tax-exempt interest occurring by reason of a short-sale. Regulatory authority will permit the Treasury to extend these rules to other transactions when appropriate. This provision applies to payments in lieu of dividends or tax-exempt interest made after December 31, 1984.

g. Reporting of State income tax refunds

State and local governments are required under present law to provide information to the Internal Revenue Service on refunds of State or local income tax, and to supply a copy to the taxpayer in January of the following year. Under temporary regulations, the Treasury Department has provided that reporting is not required when the officer making the refund determines that the individual receives no Federal tax benefit from the tax payment to which the refund relates. The conference agreement codifies the provisions of the temporary regulations providing exceptions from the requirements of the reporting to individuals.

h. Backup withholding

The conference agreement provides that, with respect to backup withholding, the Secretary's authority to require that a payee certify under penalties of perjury that his taxpayer identification number is correct is limited to interest, dividends, patronage dividends, and amounts subject to broker reporting.

3. Other compliance provisions

a. Modifications to charitable contribution rules; incorrect valuation penalties

Present law provides expressly that a charitable contribution is deductible only if verified in the manner required by Treasury regulations (Code sec. 170(a)(1)). The conference agreement requires Treasury to issue such regulations, before January 1, 1985, requiring individual donors to obtain an independent, qualified appraisal (and attach a summary of the appraisal, signed by the qualified appraiser, to the return) where the claimed value of donated property, other than publicly traded securities, exceeds certain dollar amounts (generally, $5,000). Also under such regulations, if the donee charity sells donated property for which an appraisal is required within two years after receipt, the charity must file an information report on such sale with the IRS (with a copy to the donor). These substantiation and reporting rules apply to contributions made after December 31, 1984.

The conference agreement generally amends the present-law penalty for valuation overstatements (sec. 6659) by deleting the exception for property held for more than five years, and by extending the penalty to incorrect valuations for estate and gift tax purposes. Also, in the case of charitable contribution deduction overvaluations only, the conference agreement increases the section 6659 penalty to a flat 30 percent of the tax liability understatement where the claimed valuation is 150 percent or more of the correct value, and provides that the penalty cannot be waived by the IRS unless (in addition to the waiver requirements of present law) the claimed value was based on a qualified appraisal made by a qualified appraiser and the donor made a good faith investigation of value. These modifications apply to returns filed after December 31, 1984.

b. Regulation of appraisers

Present law allows the Treasury to regulate the practice of attorneys and accountants who appear before the Treasury. No comparable authority exists with respect to appraisers. The conference agreement provides authority for the Treasury to bar disreputable appraisers from practice before the Treasury.

c. Tax deposits

The conference agreement requires taxpayers required to deposit more than once a month to make any deposit of $20,000 or more on or before the due date of the deposit. They may no longer treat deposits mailed two days in advance of the due date as timely made.

d. Interest on penalties

The conference agreement provides that interest shall be charged on the penalties for failure to file, valuation overstatement, valuation understatement, and substantial understatement of tax as if the penalties were assessed on the due date of the return (with extensions).

e. False withholding certificates

Language in the criminal penalty with respect to false withholding information which provides that no other penalty may apply is eliminated.

f. Tax litigation

The present law penalty (expanded in 1982) for maintaining dilatory Tax Court actions is made applicable to all cases pending 120 days after enactment. Title 18 is amended to provide for appropriate venue of multi-party criminal tax litigation.

g. Changes in accounting methods

The conference agreement precludes a taxpayer from asserting that the Internal Revenue Service has not consented to a change in accounting method as a defense to any penalty unless the taxpayer has requested permission to change methods.

h. Statute of limitations relating to contributions to the capital of a corporation

Present law provides an exclusion from income for certain payments to a utility in aid of construction if expenditures are made in the following two years. The conference agreement provides that the statute of limitations does not expire before the expiration of 3 years from the date the Secretary is notified concerning whether or not the contribution has been expended in the manner required.

K. Depreciation and Related Provisions

1. Real estate depreciation

Under present law, real estate can generally be depreciated, on an accelerated basis, over 15 years. The conference agreement provides that new or used real property, other than low-income housing, is to be depreciated over not less than 18 years under tables to be prescribed by the Treasury. Such tables are to use a mid-month convention. Special rules are provided for components.

Subject to transitional rules, the provision is applicable with respect to property placed in service by a taxpayer after March 15, 1984. (June 22, 1984, in the case of the mid-month convention.)

2. Depreciation recapture and installment sales

Under present law, the installment sale rules generally override the depreciation recapture rules applicable to real and personal property. Thus, generally, no real or personal property depreciation recapture income is recognized in an installment sale until the taxpayer receives installment obligation payments. Under the conference agreement, all such depreciation recapture income realized is to be recognized at the time of the installment sale. Gain in excess of such recapture income is taken into account under the installment method.

Subject to a transitional rule, the provision applies to installment sales after June 6, 1984.

3. Movies and sound recordings

Under present law, it is unclear whether movies (including video tapes) qualify as recovery property. Furthermore, taxpayers have taken the position that movies can be depreciated on the income forecast method or a similar method and still be eligible for a 10-percent investment credit. Under the conference agreement, movies cannot qualify as recovery property and are eligible for the investment credit only under the special investment credit rules applicable to certain movies.

Subject to transitional rules, the provisions are effective as of the effective date of the rules defining recovery property.

Under present law, it is unclear whether sound recordings qualify as tangible personal property for depreciation and investment credit purposes. The conference agreement provides that any sound recording may, by election, be treated as 3-year property and eligible for a 6-percent investment credit or, if the taxpayer fails to so elect, depreciated under the income forecast method or a similar method with no investment credit. Special rules are provided for contingent amounts, foreign production costs, and certain other items. Sound recordings distributed outside the United States are not subject to the tax-exempt entity leasing provisions of the conference agreement.

The provisions are generally effective for sound recordings placed in service after March 15, 1984.

4. Three-month window for new property for tax credit purposes

The 3-month window applicable in determining whether property is new property for purposes of the regular investment credit is made applicable for energy credit purposes as well. The 3-month window rule is also clarified.

The provisions are effective for property placed in service after April 11, 1984.

L. Miscellaneous Tax Reform Provisions

1. Inclusion of tax benefit items

Under present law, an individual taxpayer who receives a State tax refund may exclude from income an amount equal to the excess of the zero bracket amount over the taxpayer's other itemized deductions for the year in which the State taxes were deducted. This exclusion is permitted even though the deduction of this amount in the prior year resulted in a tax benefit.

The conference amendment provides that where a taxpayer recovers a previously deducted amount, the recovered amount is excluded from gross income only to the extent such amount did not reduce income subject to tax. This provision will apply to amounts recovered after 1983.

2. Low-interest and interest-free loans

Under present law, an interest-free or low-interest loan (below-market loan) to a family member results in a gift from the lender to the borrower for Federal gift tax purposes. To date, no court has directly held that such a loan also has any income tax consequences. Although the Internal Revenue Service has taken the position that, in general, a below-market loan to an employee or shareholder results in an economic benefit that should be included in income for Federal income tax purposes, the Tax Court has consistently held that these non-family below-market loans do not result in taxable income.

The below-market loan provision of the conference agreement requires recharacterization of below-market loans in cases where there is serious potential for tax avoidance. Where the conference agreement applies, the parties are treated as if (1) interest is charged and (2) the lender made a gift or other payment to the borrower which, in turn, is used by the borrower to pay the interest. A statutory interest rate is provided. Under *de minimis* rules, loans of $10,000 or less generally are not subject to the provision, unless a principal purpose of the interest arrangement is the avoidance of any Federal tax.

The conference agreement applies to the following enumerated categories of loans:

(1) Gift loans used to shift income between related taxpayers, such as family loans;

(2) Compensation-related loans used to avoid employment taxes or limits on the deductibility of investment interest;

(3) Corporation-shareholder loans used to claim deductions for dividends, or to circumvent other corporate tax rules; and

(4) Tax avoidance loans which are other loans if a principal purpose of the interest arrangement is the avoidance of any Federal tax.

In addition, under the conference agreement, the Treasury is authorized to promulgage regulations providing for the application of the provision to loans other than those described above. These regulations will apply the provision only in cases in which the interest arrangement has a significant effect on the tax liability of the lender or the borrower. Any loan recharacterized under the regulations will be treated under the general rules, so that interest will be imputed at the statutory rate and, in effect, rebated by the lender to the borrower. Finally, authority is provided for Treasury to issue regulations exempting from the provision classes of loans otherwise subject to the provision if the interest arrangements do not have a significant effect on the tax liability of the lender or the borrower.

The conferees also make it clear that a loan under a Federal rural low-income housing program (e.g., the FmHA section 515 program) that provides for a market rate of interest, and a reduction in loan payments to compensate the borrower for the lower rents charged is not to be considered below-market interest rate loan, provided the principal balance of the loan is amortized in accordance with the market rate of interest.

The conference agreement applies to term loans made after June 6, 1984, and amounts outstanding on demand loans after such date. Amounts outstanding on demand loans on June 6, 1984, will not be subject to the provision if repaid prior to 60 days after the date of enactment. Advances to continuing care facilities by residents to such facilities made prior to June 6, 1984, are not subject to the provision.

3. Income averaging

Income averaging is presently available to taxpayers with "averageable income." Averageable income is current year taxable income in excess of 120 percent of average taxable income in the four preceding years. In effect, income averaging widens the tax brackets by a factor of five with respect to averageable income.

The conference agreement increases the 120-percent requirement to 140 percent and provides that only the three preceding years are to be taken into account. The conference agreement modifies income averaging so that it, in effect, widens the tax brackets by a factor of four, not five, with respect to averageable income.

These changes are effective for taxable years beginning after December 31, 1983.

4. Limitations on luxury automobiles and personal use of business property

Present law provides for deductions for the expenses of operating an automobile or other business property in connection with business use, except to the extent used for entertainment purposes. The conference agreement provides that the maximum investment tax credit that can be claimed with respect to an automobile is $1,000 and the maximum depreciation that can be claimed is $4,000 in the year it is placed in service and $6,000 in any other year. The conference agreement provides that unless business use of an automobile or other specified business property is more than 50 percent of total use, the investment tax credit and accelerated cost recovery system deductions (ACRS) are not allowed. Instead, the taxpayer must use a straight-line depreciation method and a longer useful life. This provision is effective for property purchased, or leases entered into, after June 18, 1984. The conference agreement also requires that adequate contemporaneous records, such as logs of business use of an automobile, be kept, effective in 1985.

5. Treatment of certain related party transactions

The conference agreement amends the related party rules (sec. 267) so that a taxpayer would generally be placed on the cash method of accounting for purposes of deducting business expenses and interest owed to a related party cash basis taxpayer. These rules will be extended to amounts accrued by a partnership to its partners and vice versa.

Also, the conference agreement provides loss deferral and accrual provisions to transactions between corporations which are members of a controlled group of corporations, using a 50-percent control test.

These provisions generally will apply to taxable years beginning after 1983. However, the provision will not apply to (1) interest on indebtedness incurred on or before September 29, 1983, or incurred pursuant to a contract binding on that date and all times thereafter and (2) other expenses made pursuant to a contract which was binding on September 29, 1983, and at all times thereafter.

6. Section 1231 property

The conference agreement provides that gains from the disposition of business property will be treated as ordinary income to the extent of ordinary losses from the sale or exchange of such property in the previous 5 years.

The provision will be effective for taxable years beginning after December 31, 1984.

7. Use of related party structures to reduce tax on coal operations

Under present law, taxpayers may reduce the effective rate of tax on coal mining operations by establishing related party structures to take advantage of the capital gains treatment provided in section 631(c). The Code expressly prohibits such multi-party structures in the case of iron ore. The conference agreement extends the related party prohibition to coal royalties, effective for sales dispositions after September 30, 1985, except for coal sold under certain fixed contracts prior to January 1, 1990.

8. Taxation of Federal Home Loan Mortgage Corporation

The conference agreement repeals the tax exemption of the Federal Home Loan Mortgage Corporation ("Freddie Mac"), effective January 1, 1985.

9. Transfers of depreciable property between related parties

The conference agreement treats patent applications as depreciable property for purposes of characterizing income under section 1239, and treats a taxpayer and a trust in which the taxpayer has a beneficial interest as related persons, effective March 1, 1984.

10. Application of related party rule to certain tax rovisions

Present law (sec. 265(2)) disallows a deduction for interest on debt used to purchase or carry tax-exempt obligations. The application of this rule to related parties is unclear.

The conference agreement provides that the Treasury Department is to prescribe such regulations as may be necessary or appropriate to prevent the avoidance of tax under provisions (including section 265(2) and other provisions) which deal with (1) the linking of borrowing to investment, or (2) diminishing risks, through the use of related persons, pass-through entities, or other intermediaries. For purposes of section 265(2), related persons will include (1) a husband and wife, (2) a person and certain 80-percent entities with respect to such person, and (3) in appropriate cases, a person and any minor children of such person. No inference is intended that any other code provision may be circumvented by the use of related parties, pass-through entities, or other intermediaries, or that any provision (including section 265(2)), by its own terms, is not applicable in such cases. The related party rule will not operate to disallow a deduction merely because one corporation borrows in the ordinary course of business and an affiliated bank or insurance company holds tax-exempt obligations.

The provision regarding related parties, pass-through entities, and other intermediaries is generally effective on the date of enactment; however, for purposes of section 265(2) only, this provision is to be effective with respect to (1) term obligations incurred after the date of enactment, and (2) demand obligations outstanding 60 days after the date of enactment.

II. LIFE INSURANCE TAX PROVISIONS

A. Life Insurance Company Taxation

Under present law, life insurance companies may be taxed on different tax bases. As a consequence, different companies derive varying degrees of benefit from the various special deductions generally allowable only to life insurance companies and from the reserve computation rules of present law.

In lieu of the present law three-phase pattern of taxation which applies to life insurance companies, the conference agreement provides a new single-phase tax structure. This structure embodies the tax rules applicable to corporations generally except that certain special rules apply to address issues unique to the life insurance industry.

1. Computation of the deduction for reserves

Under the conference agreement, deductions for additions to reserves more closely reflect each company's liabilities to policyholders than do solvency reserves used for State law purposes. Further, the deductions are computed on the basis of uniform rules regardless of the particular assumptions used for purposes of computing statutory reserves.

Under these rules, a life insurance company can deduct an amount equal to the excess of the higher of (1) the net surrender value of the contract or (2) the federally prescribed reserve of the contract, over the amount of the reserve for tax purposes at the end of the prior year. The Federally prescribed reserve is the reserve computed using assumptions that generally reflect the highest interest rates and most recent mortality tables permitted to be used under most State laws. Companies that have traditionally used the net level term method of computing reserves with respect to noncancellable accident and health insurance contracts may continue to use that reserve method.

2. Limitation on mutual company deductions

A mutual life insurance company is owned by its policyholders. These policyholders receive distributions from the company which may represent price reductions or other policyholder benefits, interest, or returns on the policyholders' investment in the enterprise.[1] Under the conference agreement, amounts distributed by a mutual company to policyholders are, in effect, fragmented, and no deduction is allowed at the company level for amounts distributed to policyholders in their capacity as owners of the company. This is accomplished by means of an ownership differential provision. Under this provision, each mutual company's deductions for payments and credits to policyholders are reduced by the amount of an imputed return on the company's equity. There is a special 5-year transition rule for certain mutuals with much higher than average equities.

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[1] In contrast, a stock life insurance company is owned by shareholders. Although a stock company may pay policyholder dividends to its policyholders, such amounts would generally include only price reductions and policyholder benefits.

The conference agreement also mandates a study in which the Treasury would analyze the operation of the ownership differential provision in its first 3 years.

3. Stock life insurance subsidiaries of mutual companies

As a general rule, under the conference agreement, a stock life insurance subsidiary of a mutual life insurance company is treated as a stock company for tax purposes. However, for purposes of computing the limitation on mutual company deductions, the equity of a stock subsidiary is included in the mutual parent.

4. Special rule for small companies

Under the conference agreement, a small life insurance company is allowed a deduction equal to 60 percent of the first $3 million of its otherwise taxable income. This deduction phases out as otherwise taxable income increases from $3 million to $15 million. The amount of this deduction is computed on the basis of a controlled group and does not apply to income related to noninsurance activities. Generally, a small company is one the assets of which (computed on the basis of an affiliated group including both insurance and noninsurance members) are less than $500 million.

5. Rate reduction

All life insurance companies are allowed a deduction equal to 20 percent of their otherwise taxable income (reduced by the small company deduction). This deduction is computed on the basis of a controlled group and does not apply to income related to noninsurance activities.

6. Tax-exempt income

Under present law, liabilities to policyholders are treated as funded proportionately out of taxable and tax-exempt income. The conference agreement generally continues this approach.

7. Reinsurance

The provision under which the Treasury is granted authority to allocate and recharacterize income, deductions, assets, reserves, credits, and other items in the case of related party reinsurance contracts is retained and broadened in its application. Also, the Treasury is given authority to make adjustments to eliminate significant tax avoidance effect in the case of unrelated party reinsurance contracts.

8. Definition of a life insurance company

For purposes of determining whether a company qualifies as a life insurance company, funds held with respect to contracts that do not involve permanent purchase rate guarantees are not to be treated as insurance reserves.

9. Variable contracts

The conference agreement eliminates capital gains on assets held for variable contracts, generally. It also gives authority to Treasury to prescribe diversification standards for funds underlying variable contracts, with a safe harbor for funds that meet the diversification requirements of a regulated investment company (provided no more than 55 percent of the fund's assets are in cash items).

10. Effective date

Generally, the effective date for provisions dealing with the taxation of life insurance companies is January 1, 1984. Income that would otherwise result from recomputation of reserves (including section 818(c) recomputations and statutory-to-tax recomputations) and the change in accounting for policyholder dividends at the beginning of 1984 is forgiven under the conference agreement.

The amount of deferred gain from operations held in the policyholder surplus account of the company (the Phase III account) is frozen at its 1983 year-end level and distributions from such account will be taxed when distributed under the present law rules, which are retained.

Treasury's authority over related party reinsurance contracts is effective for risks reinsured on or after September 27, 1983, and over unrelated party reinsurance contracts for risks reinsured after December 31, 1984.

B. Life Insurance Products

1. Definition of life insurance

Present law does not contain a definition of life insurance or of a life insurance contract. It does, however, contain temporary rules for purposes of determining whether benefits paid under certain flexible premium products qualify as life insurance benefits exempt from income tax. The conference agreement adopts a definition that is based on the temporary rules contained in present law. A contract is treated as a life insurance contract if it meets (1) a "cash value accumulation" test, or (2) a "guideline premium" and "cash value corridor" test. Under the cash value accumulation test a contract qualifies if the cash surrender value accumulated under the contract does not exceed the cash surrender value which would arise in a traditional whole life policy assuming a reasonable interest rate is used in computing cash surrender value. Under the guideline premium limitation, contracts are disqualified if the amount of the policyholder's investment in the contract exceeds a traditional level of investment. The cash value corridor disqualifies contracts which build up excessive amounts of cash surrender value relative to life insurance risk. Generally, the new definition applies to contracts issued after December 31, 1984, except for certain increasing death benefit policies which must satisfy new rules starting on July 1, 1984. The temporary rules for flexible premium products are also extended through 1984.

For contracts that fail to meet the definition at any time, the pure insurance portion of the contract (i.e., the difference between the face amount and the cash surrender value) will be treated as term life insurance. The cash surrender value will be treated as a currently taxable deposit fund.

2. Annuities

Under the conference agreement, the present law exception from the 5-percent penalty for distributions of income allocable to investments within 10 years is repealed. Thus, the penalty generally will apply to distributions prior to age 59-1/2. In addition, if the owner of a deferred annuity dies prior to annuitization, the income in the annuity must be distributed within 5 years unless the contract is annuitized within 1 year or the beneficiary receiving ownership of the annuity contract is a spouse.

3. Group-term life insurance

The anti-discrimination rules and the $50,000 limitation on the exclusion from income of premiums for group-term benefits are extended to retired employees. For plans not in existence on January 1, 1984, these rules are effective for taxable years beginning after 1983. The extension of the $50,000 limitation will not apply to group plans existing on January 1, 1984, for any covered individual who was employed under the plan during 1983 (or was retired by January 1, 1984) and was 55 years or older on January 1, 1984. The new anti-discrimination rules will apply to existing plans starting on or after January 1, 1987, for employees retiring after that date.

III. CHARITABLE DEDUCTION RULES; PRIVATE FOUNDATION PROVISIONS; EXEMPT ORGANIZATIONS

A. Charitable Deduction Rules

1. Nonoperating (grantmaking) foundations

Under present law, contributions by individuals of cash or property to private nonoperating foundations (and certain other charitable organizations) generally are deductible up to 20 percent of the donor's adjusted gross income (Code sec. 170(b)(1)(B)), with no carryover of excess contributions. The conference agreement raises this limitation to 30 percent for gifts of cash and ordinary-income property (retaining the 20-percent limitation for all gifts of capital-gain property), and makes excess contributions eligible for a five-year carryover.

The conference agreement also provides that contributions to private nonoperating foundations of certain appreciated stock are deductible at the stock's fair market value (rather than at the present-law limitation of the donor's basis plus 60 percent of the appreciation). The increased deduction applies only to donations of up to 10 percent of the stock of a corporation for which (on the contribution date) market quotations are readily available on an established securities market.

The percentage limitation and carryover provisions of the conference agreement apply to contributions made in taxable years ending after the date of enactment. The increased deduction for contributions of certain appreciated stock applies to contributions made after the date of enactment and before January 1, 1995.

2. Expansion of circumstances in which a deduction may be claimed for qualified conservation contributions

Present law permits a deduction for contributions of qualified property interests for conservation purposes if certain requirements are satisfied. One of these requirements is that surface mining must be prohibited on the property with respect to which the contribution is made. The conference agreement repeals the surface mining prohibition if the following two requirements are satisfied: (1) the surface and mineral estates in the property were separated before June 13, 1976, and (2) the probability of surface mining occurring on the property is so remote as to be negligible.

This provision is effective for transfers after the date of enactment.

3. Charitable expense deduction for use of automobile

The conference agreement increases, from 9 cents to 12 cents per mile, the standard mileage rate allowed as a charitable deduction (if the actual expenses method is not used) for use of a passenger automobile in rendering services to a charitable organization, effective January 1, 1985.

B. Private Foundation Provisions

1. Excise tax on investment income

The conference agreement reduces from two to one percent the rate of the excise tax on net investment income of private foundations (sec. 4940), effective for post-1984 taxable years, but only if the foundation's payout for charitable purposes (computed as a five-year average) is increased by an equivalent amount.

Also, the conference agreement provides that a private operating foundation (such as a museum or library) which previously had been publicly supported for at least 10 years (or qualified as an operating foundation on January 1, 1983), which has a governing body broadly representative of the general public (with at least 75 percent consisting of persons unrelated to the foundation), and none of whose officers otherwise are disqualified persons, is exempt from the two-percent excise tax on net investment income, effective for taxable years beginning after 1984.

2. Mandatory payout rules

Under present law, a private grantmaking foundation generally must make charitable payouts ("qualifying distributions") at least equal to five percent of the fair market value of its net investment assets (Code sec. 4942). Administrative expenses incurred in making grants to other charities or in directly engaging in the active conduct of charitable activities count, without limitation, toward satisfying the five-percent payout requirement, and hence may reduce the amounts which the foundation actually distributes to charitable beneficiaries.

Under the conference agreement, a grantmaking foundation must actually pay out amounts equal to 4.35 percent of its payout base (net investment assets) as grants or contributions, expenditures (including qualifying administrative costs) incurred directly for the active conduct by the foundation of exempt activities of the foundation, or program-related investments (including qualifying administrative costs of making such investments). Other administrative expenses, including those incurred by the foundation in making grants or contributions, do not count toward the new 4.35-percent payout requirement; however, reasonable and necessary grant administrative expenses can be added to that amount in meeting the overall five-percent qualifying distributions requirement. (The new payout computation is made on the basis of a three-year average.) This modification to the present-law payout requirement is effective for taxable years beginning after 1984, but will not apply to taxable years beginning after 1990.

3. Divestiture of excess business holdings

In the case of an unusually large gift or bequest after 1969 of diverse or complex excess business holdings, the conference agreement provides the IRS with discretionary authority to permit an additional five-year period for divestiture on a showing by the foundation of diligent efforts to dispose of the holdings within the five-year period permitted under present law, but that divestiture had not been possible because of the size and complexity or diversity of the holdings. This provision applies with respect to business holdings as to which the initial five-year divestiture period ends after October 31, 1983.

The conference agreement generally retains the divestiture rules of present law (sec. 4943) with respect to "grandfathered" excess business holdings which were held by private foundations on May 26, 1969. The conference agreement includes provisions modifying the divestiture requirements with respect to the "downward ratchet" rule, eligibility for the 20-year first divestiture phase, the period for certain required divestitures in the second and third phases, technical correction in the description of the Herndon Foundation, and the treatment of an ESOP as a disqualified person for purposes of the divestiture rules applicable to holdings acquired under a pre-1969 will.

4. Expenditure responsibility and reliance rules

The conference agreement exempts from the expenditure responsibility requirements imposed on foundation grantors (sec. 4945) grants to those private operating foundations which the conference agreement exempts from the two-percent excise tax on net investment income (see above), effective for post-1984 grants.

The Treasury Department is to review its expenditure responsibility regulations for purposes of modifying requirements which are found to be unduly burdensome or unnecessary, and is to modify the required grantor reports to the IRS. Also, Treasury regulations are to be amended to extend to five years the advance ruling period during which qualifying new organizations may be considered public charities, and to permit greater reliance on IRS classifications of new charitable organizations in the first five years of their existence and in any other circumstances in which Treasury concludes that greater reliance is appropriate.

5. Abatement of first-tier penalty taxes

The conference agreement provides the IRS with discretionary authority to abate the automatic first-tier penalty taxes (other than the sec. 4941 tax on self-dealing) if the foundation establishes that the violation was due to reasonable cause and not to willful neglect, and corrects the violation. This provision applies to taxable events occurring after 1984.

6. Definitions

The conference agreement provides that the lineal descendants who are considered members of the family of a substantial contributor or other disqualified person, and thus themselves are considered to be disqualified persons (sec. 4946), are limited to the individual's children, grandchildren, great-grandchildren, and their spouses, effective January 1, 1985.

In addition, the conference agreement provides rules under which a person's status as a substantial contributor (sec. 507(d)) terminates in certain circumstances after 10 years with no connection to the foundation, effective for post-1984 taxable years. Also, the conference agreement provides special retroactive relief from the excise tax on self-dealing in a particular case where continued status as a disqualified person had triggered tax on a 1978 transaction, provided that the foundation received fair market value.

7. Public disclosure requirements

The conference agreement provides that, beginning in 1985, private foundation notices which must be published annually in a newspaper (sec. 6104(d)) are to include the telephone number of the foundation's principal office. Also, the IRS is directed to enforce fully the present-law rules concerning Form 990-PF information returns.

C. Exempt Organizations

1. Acquisition indebtedness of certain educational institutions

Under present law, tax-exempt organizations (including qualified pension trusts and IRAs) generally are subject to tax on income from a trade or business that is unrelated to the organization's exempt purposes, with exclusions for certain types of passive income. Income that is subject to tax includes income from debt-financed property. A special exception is provided for real property acquired or improved by a qualified pension trust if the acquisition satisfies certain restrictions.

The conference agreement extends the special exception to the debt-financed property rules to certain educational institutions (and certain affiliated support organizations). For any organization (including a qualified pension trust) to qualify for the exception, certain additional restrictions must be met. This provision generally is effective with respect to indebtedness incurred after the date of enactment. Certain transition rules are provided.

2. Exemption from UBIT for certain gambling income

The conference agreement exempts from the unrelated business income tax (sec. 513) income derived by nonprofit organizations from conducting certain games of chance, provided that State or local law as of October 5, 1983, permits such games to be conducted only by nonprofit organizations. This provision applies retroactively to games of chance conducted after June 30, 1981.

3. Tax status of nonprofit child care organizations

The conference agreement provides that nonprofit day care centers qualify for tax-exempt status (under sec. 501(c)(3)), and are eligible to receive tax-deductible contributions, if both (1) substantially all of the dependent care provided to children by the organization is for the purpose of enabling individuals to be gainfully employed, and (2) the services provided by the organization are available to the general public. This provision is effective for taxable years beginning after the date of enactment.

4. Church tax examinations

Present law provides that the IRS may examine church books of account (i.e., financial records) only to the extent necessary for a determination of tax. The IRS also is required to provide special advance notice before examining church books of account.

The conference agreement provides several new statutory procedures applicable to examinations of churches. Under these procedures, the IRS may commence an examination of church tax liabilities only if an IRS regional commissioner reasonably believes that the church is not tax-exempt or has taxable income. The IRS will be required to provide expanded notice before examining church records and to offer a pre-examination conference to church officials. In addition, an examination of church tax liabilities generally will be required to be completed within two years after it is commenced. These provisions are effective for church tax examinations commencing after December 31, 1984.

IV. TAX SIMPLIFICATION PROVISIONS

1. Estimated income tax for individuals

The individual estimated income tax rules of present law are simplified and clarified by the bill. Generally, an individual will be required to make estimated tax payments (including withholding payments) equal to the lesser of 80 percent of the current year's tax or 100 percent of the prior year's tax; penalties will be based on the underpayment from this amount. Payments based on annualized income will be allowed. The Secretary may waive the penalty for failure to make payments by reason of a casualty, disaster or other unusual circumstance where it would be inequitable to impose the penalty. Estimated tax payments of the alternative minimum tax will be required.

The provision will generally be effective for taxable years beginning after 1984.

2. Domestic relations

a. Transfers of property between spouses or incident to divorce

Under present law, gain is recognized on certain transfers of property in exchange for marital rights of a spouse or former spouse. The bill provides that property transfers between spouses or, if incident to divorce, between former spouses, will not result in the recognition of gain or loss. The transferee will hold the property at the transferor's basis. Also, investment tax credits will not be recaptured.

The provision generally will be effective for transfers after the date of enactment of the conference agreement. The conference agreement also allows taxpayers to elect to have this provision apply to transfers after December 31, 1983, and on or before the date of enactment.

b. Alimony

Under present law, alimony is deductible by the payor and includible in the income of the payee. The conference agreement revises the rules relating to the definition of alimony. Generally, only cash payments that will terminate on the death of the payee spouse will qualify as alimony. Alimony payments, if in excess of $10,000 per year, generally must be payable for at least 6 years and must not decline by more than $10,000. The present law requirement that the payment be based on a legal support obligation will be repealed. Payors will be required to furnish to the IRS the social security number of the payee spouse. A $50 penalty for failure to do so will be imposed.

The provision generally will be effective for divorce or separation agreements or orders executed after 1984.

c. Dependency exemption

The conference agreement provides that the $1,000 dependency exemption for a child of divorced or separated parents generally will be allocated to the custodial parent unless the custodial parent signs a written declaration that he or she will not claim the exemption for the year. Each parent may claim the medical expenses that he or she pays for the child, for purposes of computing the medical expense deduction.

Income from certain sheltered workshops will not be taken into account in determining the dependency exemption.

The provision will be effective for taxable years beginning after 1984.

d. Innocent spouse relieved of liability in certain cases

Under present law, a spouse may be relieved of liability where he or she signs a joint return and there was a substantial omission of income attributable to the other spouse. The conference agreement extends these rules to situations involving claims of grossly erroneous deductions and credits and replaces the substantial omission of income test with a substantial understatement of tax test. Also, the conference agreement overrides community property laws in certain situations where it is equitable to do so.

e. Gift and estate tax treatment of certain property settlements

The conference agreement conforms the estate tax treatment with respect to transfers of property to a former spouse under certain property settlements with the present law allowing a gift tax exemption for such transfers. The conference agreement also extends the period to enter into a property settlement agreement in order to avoid gift tax. The provision will apply to gifts made and to estates of decedents dying after date of enactment of the bill.

3. At-risk rules

The conference agreement amends the at-risk limitation on the investment tax credit by providing that the base for the credit will be reduced by nonrecourse indebtedness related to the property (i.e., a loan on which there is no personal liability). Qualified commercial financing, defined as financing from an unrelated party regularly engaged in commercial lending where no more than 80 percent of all financing for the property is nonrecourse, will be excluded from the limitation. In the case of an S corporation, recourse financing at the corporate level that is provided by a qualified commercial lender will be considered recourse financing at the shareholder level if the debt is related to property used by the corporation in an active trade or business with at least 3 full-time non-owner employees.

The conference agreement will exempt, from both the loss limitation rules of section 465 and the investment tax credit at-risk rules, the active trade or business activities of a regular business corporation. To qualify, a trade or business must have 3 full-time non-owner employees and its out-of-pocket expenses must exceed 15 percent of gross income.

The conference agreement also requires that, for a lessee to be eligible to claim the full investment tax credit, the lessee must be at risk for rental payments the present value of which is equal to at least two times the credit percentage plus 10 percent of the fair market value of the property.

The investment tax credit provisions generally will apply to property placed in service in taxable years ending after the date of enactment of the conference agreement. The changes to the section 465 rules will apply to taxable years beginning after December 31, 1983.

4. Miscellaneous Treasury administrative provisions

The conference agreement makes a number of minor amendments relating to Treasury administrative provisions. The conference agreement simplifies certain requirements of the Treasury Department to make reports to the Congress, removes the $1 million limitation of the Treasury working capital fund, increases the authorization limit from $1 million to $10 million on the revolving fund for the redemption of real property, allows the Secretary of the Treasury to accept gifts and bequests for the Treasury Department, allows an extension of time for court review of a jeopardy assessment where the government is not promptly served, removes the $1 million limitation on the Secretary of the Treasury's special authority to dispose of obligations, allows the Internal Revenue Service a minimum of 60 days to assess unpaid taxes shown on an amended return, provides the government a lien on the assets of all financial institutions which issue an unpaid guaranteed draft for the payment of taxes, allows the disclosure of windfall profit tax returns to State tax agencies and repeals the requirement that the Secretary approve changes in taxpayer's financial reporting of the investment credit.

5. Distilled spirits administrative provisions

The conference agreement repeals the present occupational tax on manufacturers of stills and makes the present statutory requirement that the Treasury Department be notified upon removal of any still from the place of its manufacture discretionary with the Treasury. The conference agreement also modifies the rules governing allowance of drawbacks with respect to distilled spirits used for food or medicinal purposes. Additionally, the Treasury Department is authorized to disclose certain information about alcohol fuel producers to administrators of State alcohol laws. The requirement that certain containers of distilled spirits bear Government-supplied strip stamps is repealed; these containers will continue to be required to bear tamper-proof closure devices. The conference agreement also expands the circumstances in which distilled spirits can be withdrawn from bond without payment of tax for use in the production of nonbeverage (e.g., cooking) wine.

6. Tax Court provisions

The conference agreement increases the small claims case dollar limit from $5,000 to $10,000. The title of the Tax Court "commissioners" will be changed to "special trial judges". The conference agreement provides that the Tax Court may prevent public disclosure of trade secrets or other confidential information.

7. *Simplification of income tax credits*

In general, the conference agreement groups existing income tax credits into logical categories and provides uniform tax liability limitations and carryover rules. The business credits (i.e., investment tax credit, targeted jobs credit, alcohol fuels credit, and ESOP credit) will be combined into one credit and allowed up to 100 percent of the first $25,000 of tax liability and 85 percent of the remainder. The research credit will continue to be allowable against 100 percent of tax liability. A 3-year carryback and 15-year carryforward period on a FIFO basis will be allowed for the business credits.

This provision will apply to taxable years beginning after 1983.

8. *Miscellaneous tax provisions*

a. *Preferred stock eligible for small business corporation stock treatment*

Under present law, a taxpayer is allowed to deduct, as an ordinary loss, up to $50,000 ($100,000 in the case of a joint return) of loss on the disposition of certain common stock of a domestic small business corporation. The conference agreement, which applies to stock issued after the date of enactment, extends ordinary loss treatment to preferred stock of qualified small business corporations.

b. *Medical expense deduction for certain lodging*

Under present law, individuals who itemize deductions may deduct certain expenses paid for medical care to the extent the expenses exceed 5 percent of adjusted gross income. Amounts paid for transportation primarily for and essential to medical care are treated as expenses paid for medical care. Amounts paid for lodging while away from home, however, do not qualify for the deduction.

Under the conference agreement, certain expenses for lodging while away from home to receive medical care as an outpatient at a hospital or certain similar medical care facilities are treated as expenses paid for medical care, up to a limit of $50 per eligible person per day. This provision is effective for taxable years beginning after 1983.

9. *Repeal of certain obsolete provisions (deadwood)*

Three provisions (Code sections 405, 409, and 1251) are repealed as deadwood.

V. PROVISIONS RELATING TO EMPLOYERS, EMPLOYEES AND TO RETIREMENT

A. Welfare Benefit Plans

1. Employer deductions

Under present law, an employer's contribution to a fund that is part of a welfare benefit plan generally is deductible in the year paid or accrued rather than at the time the benefit is provided. In contrast, deductions for contributions to a nonqualified deferred compensation plan are not allowed until an amount is includible in the employee's income.

The conference agreement provides new rules for determining the timing and the amount of an employer's deduction for contributions to a welfare benefit plan. Under the agreement, no deduction is allowed with respect to a deferred compensation arrangement or an unfunded plan before the time the compensation or benefit is provided. In the case of a funded plan, a contribution which is otherwise deductible generally will be deductible only to the extent that it does not exceed the amount that could be deducted by a cash-basis employer who paid the benefit directly, plus a limited allowance for an addition to a reserve. The reserve limits provided under the agreement generally do not apply in the case of a fund under which no employer provides more than 10 percent of total contributions.

A reserve generally is allowed equal to the value of claims that have been incurred but which are unpaid for disability, medical, life insurance, severance pay and supplemental unemployment compensation benefits. In addition, a reserve allowing prefunding over the working lives of employees is allowed for retiree medical benefits and for the tax-free portion of retiree life insurance benefits if the plans satisfy certain requirements. An excise tax of 100 percent applies to coverage provided under plans which do not satisfy these or other requirements. Further, a special reserve is allowed for supplemental unemployment compensation and severance pay benefits, based upon past experience, and higher limits for all benefits are to be provided by regulation for collectively bargained plans.

Generally, under the agreement, employer deductions with respect to a contribution of a facility to a welfare benefit fund are allowed under the usual depreciation rules. In the case of a child care facility, 60-month amortization is provided for the depreciable element of the adjusted basis of the property. Corresponding rules are provided by the agreement in the case of a facility purchased by a welfare benefit fund.

2. *Taxes on excess reserves*

The agreement provides that income on excess reserves of a welfare benefit fund are to be subject to income tax. In the case of a tax-exempt fund, the income is to be subject to the tax on unrelated business taxable income. In the case of other funds, the income is includible in the gross income of the employer. Generally reserves are to be treated as excess reserves to the extent they exceed the level that applies in determining deduction limits. The agreement provides a transition rule, however, with respect to excess reserves to provide certain life insurance and medical benefits to retirees.

3. *Additional requirements for tax-exempt status*

The agreement provides rules prohibiting discrimination in favor of highly compensated employees by a tax exempt voluntary employees' beneficiary association (VEBA) or a group legal services organization (GLSO). The agreement also requires that a VEBA, GLSO or supplemental unemployment compensation benefit trust notify the Internal Revenue Service of a claim to tax-exempt status.

4. *Study*

The conference agreement provides for a study to be submitted to the Congress by the Secretary of the Treasury on or before February 1, 1985, of the desirability and possible means of providing minimum standards for participation, accrual, vesting, and funding of welfare benefit plans.

5. *Effective dates*

The provisions of the conference agreement relating to deductions for contributions to funded plans and taxes on excess reserves are generally effective for contributions paid or accrued taxable years beginning after December 31, 1985. The limitations affecting deductions with respect to facilities, however, generally apply after June 22, 1984, and the provision applicable to unfunded deferred compensation or unfunded benefit plans generally applies to amounts paid or incurred after the date of enactment. The provisions of the agreement relating to additional requirements for tax exempt status of such a fund apply for taxable years beginning after December 31, 1984.

B. General Pension Provisions

1. *Distribution rules for qualified plans*

Present law provides that distributions to an individual under a qualified pension, profit-sharing, or stock bonus plan ("qualified plan") prior to age 59½ are subject to an additional 10-percent income tax to the extent that the amounts are attributable to years in which the individual was a key employee in a top-heavy plan. In addition, present law requires that distributions to a key employee in a top-heavy plan commence no later than age 70½ without regard to whether the key employee has retired.

Under present law, in the case of a qualified plan or an IRA, after the death of the participant and the participant's surviving spouse, any distributions to beneficiaries must be made within 5 years after the death of the participant or surviving spouse.

Under present law, if the balance to the credit of an employee is paid as a qualifying rollover distribution from a qualified plan (or tax-sheltered annuity), all or any portion of the distribution may be rolled over, within 60 days of the date of the distribution, to another qualified plan (or tax-sheltered annuity) or to an IRA. No rollover is permitted for a plan distribution that is not a total distribution.

Under the agreement, the additional 10-percent income tax applies to amounts attributable to years in which the individual was a 5-percent owner of the employer without regard to whether the plan was top heavy. Rollovers to IRAs of certain partial distributions under a qualified plan are permitted. In addition, the agreement provides that distributions are to commence at age 70 1/2 to all 5-percent owners of the employer.

The agreement changes the after-death distribution rules to provide that the 5-year rule is satisfied under a qualified plan or an IRA if (1) an immediate annuity contract is distributed to the beneficiary or (2) an annuity is paid from or under the plan. Similar rules are provided for annuity contracts (including tax-sheltered annuities).

The provisions generally are effective for plan years beginning after December 31, 1984. The provisions relating to rollovers of partial distributions apply to distributions made after the date of enactment, in taxable years ending after that date.

2. *Treatment of distributions of benefits substantially all of which are derived from employee contributions*

Under present law, an employee-contribution only plan may be a qualified plan. In addition, nondeductible employee contributions to a qualified plan may be withdrawn at any time without penalty. The first withdrawals before an annuity commences are treated as a return of any nondeductible contributions, which are not includible in gross income.

Under the agreement, in the case of a plan in which more than 85 percent of total contributions during a representative period are employee contributions, the first amounts withdrawn from the plan are treated as coming out of earnings in the employee's account. In addition, if an employee receives a loan (directly or indirectly) under the plan, the agreement treats the amount of the loan as a distribution under the plan.

The provision is effective for any withdrawals occurring, or loans made, more than 90 days after the date of enactment.

3. *Provisions relating to top-heavy plans*

Under present law, if a qualified plan is top heavy, then certain minimum requirements must be met. These requirements include rules relating to the provision of minimum benefits or contributions to non-key employees.

Under the conference agreement, the definition of a key employee is amended to exclude officers who earn less than 150 percent of the dollar limit on annual additions under a defined contribution plan ($45,000 for 1984). The accrued benefit of any individual is disregarded after the individual has been separated from service for 5 years. Under the conference agreement, employer contributions made pursuant to a salary reduction arrangement are counted for purposes of the top-heavy plan rules. The conference agreement exempts governmental plans from the top-heavy plan rules. In addition, a simplified amendment procedure applies if the Secretary fails to issue final regulations with respect to the top-heavy plan requirements by January 1, 1985.

The provisions generally are effective for plan years beginning after December 31, 1983. The rules relating to separated employees and salary reduction arrangements are effective for plan years beginning after December 31, 1984.

4. Repeal of estate tax exclusion for qualified pension plan benefits

TEFRA reduced the estate tax exclusion for certain benefits under qualified plans, and IRAs, and military retirement benefits to $100,000, for decedents dying after December 31, 1982.

Under the conference agreement, the separate estate tax exclusion for retirement benefits is repealed, effective for decedents dying after December 31, 1984. A transition rule is provided for this change and for the TEFRA change with respect to certain participants whose benefits were in pay status as of the effective date of either provision.

5. Affiliated service groups, employee leasing arrangements, and collective bargaining agreements

Under present law, certain aggregation rules apply to treat employees of related employers as if they are employed by a single employer for purposes of the qualified retirement plan provisions and certain other benefit provisions. Thus, all employees of employers that are members of an affiliated service group are treated as employed by a single employer. Further, certain leased employees are treated as employees of the lessee unless, under a safe harbor, the leasing organization provides certain minimum benefits to the employee.

Under the conference agreement, the affiliated service group rules are changed so that the attribution-of-ownership rules include "brother-sister" relationships. Further, leased employees who are common-law employees of the lessee are treated as the lessee's employees regardless of whether the safe-harbor requirements are satisfied.

Under present law, many rules applicable to qualified plans do not apply to a plan maintained pursuant to a collective bargaining agreement. Under the conference agreement, an agreement involving an employee organization more than one-half of the members of which are owners, officers, or executives of the employer is not considered a collective bargaining agreement for purposes of these rules.

The modifications to the rules for affiliated service groups are effective for plan years beginning after December 31, 1984. The employee leasing provision is effective for plan years beginning after

December 31, 1983. The collective bargaining agreement provision is effective on April 1, 1984.

6. Standards for cash or deferred arrangements

Under present law, an employee may elect to defer compensation (within limits) under a qualified cash or deferred arrangement that is provided by a tax-qualified profit-sharing or stock bonus plan. Permitted deferrals are generally not taxed until they are distributed. In determining whether a cash or deferred arrangement meets the standards of the Code, either a special nondiscrimination standard of cash or deferred arrangements or the general nondiscrimination standard applicable to qualified plans may be applied. The general standard allows integration with social security benefits.

Under the conference agreement, a cash or deferred arrangement is to qualify (and elective deferrals are to be excluded from gross income) only if the arrangement meets the special standards provided for a qualified cash or deferred arrangement. The provision generally is effective for plan years beginning after December 31, 1984.

7. Application of cash or deferred arrangement rules to pre-ERISA money purchase pension plans

Through 1979, the tax treatment of cash or deferred arrangements under qualified plans in existence on June 27, 1974, was subject to a transition provision of ERISA. Under the transition provision, these plans were subject to the rules in effect before January 1, 1972, relating to cash or deferred arrangements. The Revenue Act of 1978 provided new rules for cash or deferred arrangements under qualified profit-sharing and stock bonus plans (sec. 401(k)), but the new rules do not apply to money purchase pension plans.

Under the conference agreement, the rules for qualified cash or deferred arrangements under qualified profit-sharing plans are made applicable to cash or deferred arrangements under certain pre-ERISA money purchase pension plans (plans in existence on June 27, 1974). The agreement provides that the rules for qualified cash or deferred arrangements apply to such a money purchase pension plan only if employer and employee contributions under the plan do not exceed the limits under the plan's contribution formula in effect on June 27, 1974.

This provision of the agreement applies for plan years beginning after the date of enactment.

8. Treatment of certain medical benefits under pension plans

Present law limits contributions and benefits under a qualified plan. Post-retirement medical benefits provided under a qualified plan are not taken into account in applying the limits.

Under the conference agreement, in the case of post-retirement medical benefits provided for a key employee, separate accounting is required and the contributions allocated to a separate account are considered employer contributions to a defined contribution plan in applying the limits. The provision applies to years beginning after March 31, 1984.

9. Alimony treated as compensation for IRA purposes

Under present law, an individual generally is entitled to deduct individual retirement arrangement (IRA) contributions up to the lesser of $2,000 or 100 percent of compensation. Under the conference agreement, all alimony received by a divorced spouse is treated as compensation for this purpose, effective for taxable years beginning after December 31, 1984.

C. Employee Benefits

1. Exclusions for certain employer-provided fringe benefits; two-year moratorium on faculty housing regulations

The Code defines gross income for income tax purposes as including "all income from whatever source derived" and specifies that it includes "compensation for services" (sec. 61). Similarly, the social security and unemployment insurance payroll taxes (FICA and FUTA) and income tax withholding generally apply to all remuneration for employment, including the cash value of any noncash remuneration. However, certain fringe benefits, such as health benefits, are expressly excluded from gross income or wages by specific statutory provisions.

A moratorium first enacted in 1978 prohibited issuance of Treasury regulations relating to the income tax treatment of nonstatutory fringe benefits. The legislative moratorium expired on December 31, 1983. The Treasury Department has announced that Treasury and the IRS "will not issue any regulations or rulings altering the tax treatment of nonstatutory fringe benefits prior to January 1, 1985," and that "present administrative practice will not be changed during this period."

Under the conference agreement, the general legislative moratorium on regulations that expired December 31, 1983, is not extended. Instead, the conference agreement sets forth statutory provisions under which (1) certain fringe benefits provided by an employer are excluded from the recipient employee's gross income for Federal income tax purposes and from the wage base (and, if applicable, the benefit base) for purposes of income tax withholding, FICA, and FUTA, and (2) any fringe benefit that does not qualify for exclusion under the bill and that is not excluded under another statutory fringe benefit provision of the Code is includible in gross income for income tax purposes, and in wages for employment tax purposes, at the excess of its fair market value over any amount paid by the employee for the benefit.

The excluded fringe benefits are those that qualify under one of the following five categories as defined in the agreement: (1) a no-additional-cost service, (2) a qualified employee discount, (3) a working condition fringe, (4) a de minimis fringe, or (5) a qualified tuition reduction for education below the graduate level. Special rules apply with respect to certain free parking or subsidized eating facilities provided to employees, on-premises athletic facilities, and demonstration use of an employer-provided car by full-time automobile salespersons. In the case of a no-additional-cost service, a qualified employee discount, a subsidized eating facility, or a qualified tuition reduction, the exclusion applies with respect to benefits provided to officers, owners, or highly compensated employees only if the benefits are also made available to other employees on a nondiscriminatory basis.

Also, the conference agreement imposes a moratorium on the issuance of income tax regulations providing for the inclusion in gross income of the excess of the fair market value of qualified campus lodging over the greater of the operating costs paid in furnishing the lodging or the rent received, applicable to qualified campus lodging furnished after December 31, 1983 and before January 1, 1986.

The provisions of the conference agreement generally take effect on January 1, 1985, except that the tuition reduction exclusion applies with respect to education furnished after June 30, 1985.

2. Cafeteria plans

Under present law, a participant in a nondiscriminatory cafeteria plan is not treated as having received a taxable benefit offered under the plan solely because the participant may choose among the taxable and nontaxable benefits offered under the plan. Proposed Treasury regulations provide that employer contributions with respect to an accident or health plan, qualified group legal services plan or a dependent care assistance program are not excluded from a participant's gross income to the extent that the participant is assured of receiving benefits under the plan without regard to whether he or she incurs covered expenses.

The conference agreement changes the cafeteria plan provisions in several respects. First, benefits provided under certain plans in existence on February 10, 1984, or for which substantial implementation costs had been incurred before that date, will not fail to be excluded under the cafeteria plan provisions of the proposed Treasury regulations, provided that these plans are not modified after that date in a way which allows additional benefits to be provided. The provision is effective for benefits provided before January 1, 1985, for all such plans. For plans under which an employee must fix the amount of contributions before the beginning of the year and under which unused contributions generally are not available to the employee until the end of the year, the provision is effective for benefits provided before July 1, 1985.

Second, the conference agreement provides that cash generally is the only taxable benefit which may be offered in a cafeteria plan and that the new fringe benefits described in the previous section (no-additional cost services, qualified employee discounts, working condition and de minimis fringes and qualified tuition reduction) may not be offered in such a plan.

Third, no more than 25 percent of total nontaxable cafeteria plan benefits may provided to key employees.

Fourth, annual reports are required from employers utilizing cafeteria plans on the cost of, and number of employees receiving, statutory fringe benefits. Additional information will be required from a sample of the employers that provide substantial benefits.

Finally, the Secretary of Health and Human Services, in cooperation with the Secretary of the Treasury, is required to submit to the Committee on Ways and Means and the Committee on Finance a study concerning the effect of the cafeteria plans on the containment of health care costs by April 1, 1985.

The provisions relating to permissible taxable benefits, proportion of benefits to key employees, and reporting requirements take effect on January 1, 1985.

D. Employee Stock Ownership Provisions

Under present law, the limit on the tax credit for employer contributions to an employee stock ownership plan (ESOP) is scheduled to increase from one-half of one percent of payroll in 1983 and 1984 to three-fourths of one percent in 1985. The conference agreement freezes the limit at the current rate through 1987.

In addition, the conference agreement provides a number of incentives for employee stock ownership. First, it permits a tax-free rollover of the proceeds from the sale of a business to an ESOP or to certain worker-owned cooperatives, provided (1) the proceeds are reinvested in the securities of another business and (2) immediately after the sale, the ESOP owns at least 30 percent of the value of employer securities. Second, a corporate deduction is allowed for dividends paid on ESOP stock, provided the dividends are paid out currently to employees. Third, a bank, insurance company, or other commercial lender is permitted an exclusion from income for 50 percent of the interest received on loans to ESOP companies, provided the loan proceeds are used to finance an ESOP's acquisition of company stock. Fourth, the conference agreement provides that the liability for estate taxes may be assumed by an ESOP in return for a transfer from the estate of stock of an equal value, provided the company sponsoring the ESOP guarantees payment of the taxes.

The provisions are effective for years beginning after December 31, 1984.

E. Miscellaneous Benefit Provisions

1. Treatment of certain distributions from a qualified terminated plan

Under present law, a distribution under a qualified plan is not a lump sum distribution eligible for a tax-free rollover to an IRA unless it consists of the balance to the credit of the employee and is made within one taxable year of the recipient.

Under the conference agreement, special relief is provided for certain plan distributions received by a taxpayer during 1976 and 1977 so that the amounts received are treated as a lump sum distribution eligible for rollover. In addition, the usual period of limitations is extended. The provision is effective upon date of enactment.

2. Special rule for Trans-Alaskan pipeline employees

Under present law, in the case of the partial termination of a qualified pension plan, the rights of all affected employees to benefits accrued to the date of the partial termination generally become nonforfeitable upon the partial termination to the extent those benefits have been funded.

Under the conference agreement, in the case of certain multiemployer pension plans located in the state of Alaska, no partial termination is deemed to have occurred merely because there was a reduction in workforce upon completion of the Trans-Alaskan pipeline. The provision is effective on the date of enactment.

3. Distribution requirements for plans, accounts and annuities of insurer in rehabilitation proceedings

Under present law, distributions to the owner of an IRA must be made by the end of the taxable year in which the owner attains 70-1/2. In addition, after the death of the owner, distributions must be made to beneficiaries within 5 years after the death of the owner. In the event that distributions are not made as required under present law, an excise tax of 50 percent applies to the amounts that are required to be distributed. Similar requirements apply to certain distributions of benefits under qualified plans and certain annuity arrangements.

Under the conference agreement, an amount is not required to be distributed under the usual rules for IRAs or qualified plans to the extent that the amounts are held by an insurance company that, on March 15, 1984, is engaged in rehabilitation proceedings under applicable State law. The provision is effective on March 15, 1984.

4. Extension of time for repayment of qualified refunding loans

TEFRA imposed limits on the extent to which an individual can borrow amounts from a qualified plan without the loan being treated as a distribution under the plan. A transition rule was provided for certain "qualified refunding loans" made on or after August 13, 1982, and repaid before August 14, 1983.

Under the conference agreement, the period for making and repaying qualified refunding loans is extended to January 1, 1985, for qualified refunding loans of non-key employees. The provision is effective as if enacted in TEFRA.

5. Incentive stock options

Under the conference agreement, the fair market value of stock, for purposes of applying the incentive stock option provisions, is to be determined without regard to restrictions which may lapse. The provision is generally effective for options granted after March 20, 1984.

6. Certain section 83(b) elections.

The time for filing an election under section 83(b) with respect to the transfers of property after June 30, 1976, and before November 18, 1982, to an individual in connection with the performance of services is extended until the time for filing the taxpayer's next tax return, where the transfer was at fair market value and the transferor consents.

7. Employer and welfare benefit fund treated as related persons

Under present law, the gain from the sale of depreciable property between certain related taxpayers is treated as ordinary income but an employer and a welfare benefit fund to which the employer contributes generally are not treated as related parties. The conference agreement treats an employer and a welfare benefit fund as related parties if the employer controls the fund directly or indirectly, effective for sales or exchanges after the date of enactment.

8. Elimination of retroactive application of amendments made by Multiemployer Pension Plan Amendments Act of 1980

The Multiemployer Pension Plan Amendments Act of 1980 (MPPAA) was enacted on September 26, 1980. That Act generally imposes liability on an employer who withdraws from a multiemployer defined benefit pension plan on or after April 28, 1980.

Under the conference agreement, an employer does not have withdrawal liability under the MPPAA as a result of a withdrawal from a multiemployer plan before September 26, 1980. In addition, withdrawal liability does not apply to a withdrawal completed before December 31, 1980, pursuant to a binding agreement in effect on September 26, 1980. Employers are entitled to a refund of amounts collected. The provision is effective on the date of enactment.

9. Pension portability involving telecommunication divestiture

Under present law, generally all years of service with the employer maintaining a qualified plan must be taken into account for purposes of the minimum participation and vesting requirements. In any case in which an employer maintains a plan of a predecessor employer, service for the predecessor is treated as service for the employer.

Under the conference agreement, the period of service of a qualified employee (an employee of AT&T or any of its subsidiaries immediately before divestiture) with any of the companies after divestiture includes service with any of the other companies whether or not that service was performed before divestiture. Accordingly, the rules provided for 1985 and thereafter by the court order requiring divestiture of certain former subsidiaries of AT&T, under which post-divestiture service with another divested company would not be taken into account, will not be effective.

10. Accrual of vacation pay

Under present law, an accrual method taxpayer may elect to accrue a deduction of an addition to a vacation pay account equal to the amount payable (but not necessarily paid) within 12 months after the close of the taxable year, regardless of when actually paid or whether the employees' right to the vacation pay is vested or contingent. The conference agreement limits the account balance to the amount expected to be paid before 12 months after the close of the taxable year, effective for taxable years beginning after March 31, 1984.

VI. TAX-EXEMPT OBLIGATIONS

A. Mortgage Subsidy Bonds

1. Extension of qualified mortgage bond program

Under the Mortgage Subsidy Bond Tax Act of 1980 (as amended), State and local governments were allowed to issue limited amounts of tax-exempt bonds to finance mortgages on owner-occupied residences. The State volume ceiling for qualified mortgage bonds was the greater of (1) 9 percent of the average area mortgage originations for single family, owner-occupied residences in the State during the preceding 3 years, or (2) $200 million. The authority to issue qualified mortgage bonds expired on December 31, 1983.

The conference agreement extends the tax-exemption for qualified mortgage bonds for four years, for bonds issued after December 31, 1983, and before January 1, 1988.

Under the conference agreement, reporting requirements, similar to the TEFRA reporting requirements for private activity bonds, are imposed on issuers of mortgage subsidy bonds (including qualified mortgage bonds and qualified veterans' mortgage bonds). The conference agreement also includes a statement of Congressional intent that issuers are expected to use qualified mortgage bonds and mortgage credit certificates (discussed below), to the greatest extent possible, to make loans available to lower-income families.

Elected officials of issuing jurisdictions are required to submit an annual statement to the Treasury Department which states the policy of the issuer in distributing proceeds of qualified mortgage bonds and mortgage credit certificates (but not qualified veterans' mortgage bonds) and evaluates the performance of the issuer's program relative to that Congressional intent.

These provisions are effective for bonds issued after December 31, 1984.

In extending the quailfied mortgage bond program, the conference agreement also extends the validity of State allocation formulas for qualified mortgage bond authority which expired on December 31, 1983. The governors of certain States are provided with interim authority to allocate their respective State volume ceilings.

The conference agreement also terminates most of the transition rules under the Mortgage Subsidy Bond Tax Act of 1980 after December 31, 1984. Additionally, bonds issued pursuant to these transition rules after June 15, 1984, and before January 1, 1985, will not be tax-exempt unless the State allocates a portion of its 1984 State qualified mortgage bond volume ceiling to those bonds.

2. Qualified veterans' mortgage bonds

Present law allows States to issue tax-exempt general obligation bonds to provide mortgages to finance residences for veterans (qualified veterans' mortgage bonds). Qualified veterans' mortgage bonds are not subject to a statewide volume ceiling and the authority to issue these bonds did not expire on December 31, 1983.

The conference agreement places new restrictions on issuance of qualified veterans' mortgage bonds. Under these restrictions, authority to issue qualified veterans' mortgage bonds is limited to programs that issued such bonds before June 22, 1984; loans made with the proceeds of qualified veterans' mortgage bonds issued after June 22, 1984, are to be limited to veterans who served in active duty before 1977; and applications for a loan to be made with the proceeds of qualified veterans' mortgage bonds must be made before the later of (a) the date which is 30 years from the date of discharge from military service, or (b) January 31, 1985. Additionally, under the conference agreement, qualified veterans' mortgage bonds may only be used to finance principal residences as defined for purposes of qualified mortgage bonds. The conference agreement further provides that the volume of qualified veterans' bonds that States may issue is limited by a formula based on the volume of such bonds issued by the States in the period January 1, 1979 through June 22, 1984.

These provisions generally are effective on the date of enactment; however, the restrictions on qualified veterans' mortgage bonds are effective for bonds issued after June 22, 1984. Bonds issued pursuant to State referenda held or authorized to be held before October 18, 1983, are exempt from the restrictions.

The conference agreement also permits the State of Oregon to borrow from the Federal Financing Bank, under specified conditions, amounts necessary to meet the debt service on certain qualified veterans' mortgage bonds.

3. Treatment of Kansas City, Missouri and Kansas City, Kansas as a unified metropolitan statistical area

The conference agreement provides that Kansas City, Missouri and Kansas City, Kansas (and surrounding counties) are to be treated as one metropolitan statistical area for tax and all other purposes of Federal law, effective on the date of enactment.

B. Mortgage Credit Certificates

The conference agreement allows State and local governments, as an alternative to qualified mortgage bonds, to exchange all or part of their qualified mortgage bond authority (as extended by the conference agreement) for authority to issue mortgage credit certificates (MCCs). Home purchasers receiving MCCs are entitled to a non-refundable income tax credit equal to a specified percentage of the interest that the homebuyer pays during the taxable year on the mortgage on his principal residence. This percentage may not be less than 10 percent or more than 50 percent of the interest on the qualifying indebtedness. In addition, the maximum credit which any taxpayer may use in a given year is limited to the greater of (i) 20 percent of the qualifying indebtedness, or (ii) $2,000. The amount of a homebuyer's interest deduction in any year is reduced by the amount of the credit for that year. Excess unused credits may be carried forward by the recipient for up to 3 years.

Eligibility to receive MCCs generally is determined on the same basis as eligibility for qualified mortgage bonds. MCCs are also to be available for certain manufactured homes and to residents of housing cooperatives who otherwise meet the applicable eligibility requirements. MCCs may be limited to residences in particular developments only if the developer certifies that the price is not increased because of the MCCs, and may not be limited to specified lenders unless this rule is waived by Treasury regulations. No MCC is allowed for loans between related parties or for loans made with tax-exempt bond proceeds.

A State may issue MCCs in an aggregate principal amount equal to 20 percent of the amount of the qualified mortgage bond authority that the State trades in for the year. However, if (1) the State volume ceiling exceeds 20 percent of the average annual amount of mortgages originated in the State during the preceding three years, or (2) the State issued less than $150 million of qualified mortgage bonds in 1983, then the weighted average size of credits issued in the State may not exceed 20 percent.

The MCC program is to be administered primarily by State and local governments, with Federal reporting requirements and appropriate penalties and fees. However, the Treasury Department has the option of adopting a centralized (i.e., national) system of administration.

The MCC program is effective for credits issued on or after January 1, 1985, using qualified mortgage bond authority for 1984 and later years. The program will sunset on December 31, 1987, together with the sunset for qualified mortgage bonds.

C. Private Activity Bonds

1. Volume limitations

Under the conference agreement, private activity tax-exempt bonds are subject to statewide volume limitations. The limitations apply to certain industrial development bonds (IDBs) and to student loan bonds issued within the State. Bonds issued to finance projects for multifamily residential rental property are exempt from the limitations. Additionally, IDBs issued to finance convention or trade show facilities, airports, docks, wharves, and certain mass commuting facilities are exempt from the limitations if the facilities are owned for tax purposes by a State or local governmental unit and the rents charged tenants are not front-loaded to achieve an effect more accelerated than a straight-line rent.

The limitations are set at the greater of $150 for each resident of the State (according to the most recent census estimates) or $200 million. The limitations will be reduced to the greater of $100 per capita or $200 million after 1986 (when the small issue IDB exception expires except with respect to manufacturing facilities). Within each State, the limitation is to be allocated among State and local issuers according to rules similar to those used for allocating qualified mortgage bond authority.

The conference agreement provides for a three-year carryover (six years in the case of pollution control bonds) of a State's volume limitation to finance specific projects or for student loan bonds. The carryover is not applicable for small issue IDBs. Additionally, for States whose 1983 volume exceeded the statewide limitation, a two-year phase-in is applicable.

This provision of the conference agreement applies generally to bonds issued after December 31, 1983. A transitional rule exempts bonds for which an inducement resolution was adopted before June 19, 1984, if the bonds are issued before January 1, 1985. Additionally, bond issues for which an inducement resolution was adopted before October 19, 1983, are to receive priority in allocation of the State's volume limitation in the year in which such bonds are issued if either construction on the project had commenced or a binding contract existed before October 19, 1983.

2. Restrictions on cost-recovery for IDB-financed property

The conference agreement repeals three of the four present law exceptions to the rule requiring straight-line cost recovery deductions (over ACRS periods) for IDB-financed property. However, the conference agreement allows projects for multifamily residential rental property to continue to receive full accelerated cost recovery deductions over ACRS periods.

Subject to certain transition rules, this provision applies to property placed in service after December 31, 1983, which is financed by obligations issued after October 18, 1983.

3. Denial of tax-exemption to Federally guaranteed bonds

The conference agreement denies tax-exemption for the interest on obligations guaranteed directly or indirectly by the Federal government, including bonds issued in connection with Federal deposit insurance. Exceptions are provided for guarantees for various housing-related agencies and student loan guarantees, for guarantees of pollution control bonds by the Small Business Administration, and for a specified program of the Bonneville Power Administration (for five years only). Bonds issued to finance multifamily residential rental property are exempt from the Federal guarantee rule.

This provision applies generally to bonds issued after December 31, 1983. The provision applies to bonds issued in connection with Federal deposit insurance after April 14, 1983, except bonds issued pursuant to a contract binding at all times after March 3, 1983.

4. Arbitrage restrictions

IDBs.—The conference agreement applies new arbitrage restrictions to IDBs in addition to the present arbitrage rules applicable to those bonds. Under these rules, after an initial temporary period (and except for temporary periods related to debt service), all bond proceeds, other than an amount that may not exceed 150 percent of annual debt service, must be applied to the governmental purpose for which the bonds are issued. All bond proceeds must be applied to the governmental purpose for which the bonds were issued. Arbitrage earned on investments that are not acquired in order to carry out a governmental purpose must be paid to the Federal government at 5 year intervals, with any remaining balance being paid 30 days after the bonds are retired. Bonds issued to finance multifamily residential rental property are exempt from these new restrictions.

A special provision is included providing that a certain State university permanent fund does not violate the arbitrage restrictions of present law or of the conference agreement as that fund is operated presently.

These rules apply to bonds issued after December 31, 1984.

Student loan bonds.—Subject to Treasury regulations, the conference agreement applies generally the same rules as the new rules provided for IDBs to student loan bonds guaranteed under the GSL program. Non-GSL student loan bonds are subjected to arbitrage rules similar to the rules applicable to qualified mortgage bonds.

The new arbitrage rules for non-GSL student loan bonds apply to bonds issued after December 31, 1985; for GSL bonds, the new rules will apply on the effective date of the new Treasury regulations.

5. Limitations on acquisition of land and existing facilities

Nonagricultural land.—The conference agreement eliminates the use of tax-exempt bonds to finance nonagricultural land if 25 percent or more of the proceeds of an issue are used for such land. This limitation is increased to 50 percent in the case of an industrial park, and exceptions are provided for certain airport and dock land acquired for expansion or pursuant to noise abatement or environmental regulations.

Agricultural land.—The conference agreement permits tax-exempt bond financing up to $250,000 per first-time farmer for agricultural land (and facilities located on such land). Additionally, used equipment may be purchased in connection with agricultural land by a qualified first-time farmer. A first-time farmer is defined as an individual who has never owned an amount of agricultural land in excess of 15 percent of the county median farm size. In no event can the value of that land exceed $125,000.

Existing facilities.—The conference agreement generally denies the use of tax-exempt bonds to finance the purchase of existing facilities. An exception is provided for the purchase of existing buildings if an amount equal to at least 15 percent of the lesser of (1) the cost of the building or (2) the amount of IDB financing is spent on rehabilitation. In the case of structures other than buildings, the rehabilitation expenditures must exceed 100 percent of the lesser of those two amounts. Where more than one building is involved, the determination of whether the rehabilitation threshold is satisfied is to be made on a project (rather than a building or structure) basis.

Effective date.—These provisions apply generally to bonds issued after December 31, 1983. A transitional rule exempts bonds issued before January 1, 1985, pursuant to an inducement resolution adopted before June 19, 1984.

6. Repeal of advance refunding for qualified public facilities

The conference agreement repeals the provision permitting advance refundings for certain convention and trade show facilities, airports, docks, wharves, and mass commuting vehicles. This provision applies to advance refunding bonds issued after the date of enactment, except for advance refunding bonds for airports and docks issued before January 1, 1985.

7. Elimination of IDB financing for certain facilities

The bill eliminates the use of tax-exempt IDBs to finance airplanes, luxury boxes, gambling facilities, alcoholic beverage stores, and health clubs. This provision applies generally to bonds issued after December 31, 1983 (in the case of health clubs, April 13, 1984). An exception applies to bonds issued to finance racetracks where an inducement resolution was adopted before June 19, 1984, and the bonds are issued before January 1, 1985.

8. Amendments to the small-issue exception

Extension of small-issue exception.—The conference agreement extends for two years, through 1988, the small issue exception for manufacturing facilities. The exception will expire on December 31, 1986, as presently scheduled, in the case of other facilities.

Aggregate limit per taxpayer for small-issue exception.—The conference agreement provides that interest on small-issue IDBs is not tax-exempt if the portion of the issue allocated to any beneficiary (when increased by all other outstanding IDBs allocated to the beneficiary) exceeds $40 million.

This provision applies generally to bonds issued after December 31, 1983. Transitional rules apply in the case of bonds issued before January 1, 1985, to finance a project for which an inducement resolution was adopted before June 19, 1984.

Aggregation of issues for single project.—The conference agreement provides that if two or more issues of bonds are to be used with respect to a single project, the issues are to be treated as one issue for purposes of applying the small-issue volume limitation. Subject to certain transitional rules, this provision applies to bonds issued after December 31, 1983.

Clarification that residential property may be in a mixed use structure.—The conference agreement clarifies that a part of a building qualifying as low -and moderate-income residential rental property may be used for nonresidential purposes, but limits tax-exempt financing to the portion of the building used for such housing. This provision applies to bonds issued after December 31, 1983.

9. Extension of substantial user rules

The conference agreement expands the definition of related party for purposes of the rule under which interest on bonds is not tax-exempt if the bonds are held by a substantial user of the facilities financed by the bonds or a related party to treat as related parties all partners of a partnership and all shareholders of an S corporation as well as spouses and dependent children or such partners and shareholders. This provision applies to bonds issued after December 31, 1983.

10. Extension of certain requirements of the Internal Revenue Code to bonds exempt from tax pursuant to other provisions of law

Extension of requirements.—The conference agreement subjects all bonds for which tax-exemption is provided outside of the Internal Revenue Code or which are excepted from any requirements of the Code to the Code rules governing tax-exempt bonds. Exceptions are provided to the income tax rules for bonds issued to finance the Alaska Railroad, the Bonneville Power Administration, and the Oregon Small Energy Bond Program.

The conference agreement clarifies that transfers of all non-Code bonds are subject to the Federal gift, estate, and generation-skipping transfer taxes. A Federal district court had ruled on April 25, 1984, that transfers of certain bonds issued pursuant to section 11(b) of the Housing Act of 1937 were exempt from Federal estate tax (*Haffner* v. *Comm'r*).

This provision applies for income tax purposes to bonds issued after December 31, 1983, except it applies to bonds issued after June 18, 1984, in the case of bonds exempt from tax under section 11(b) of the Housing Act of 1937.

In the case of the Federal gift, estate, and generation-skipping transfer taxes, the provision applies to estates of individuals dying, gifts made, and generation-skipping transfers occurring after June 18, 1984. The agreement further provides that no inference is to be drawn from the June 18, 1984, effective date that transfers of non-Code bonds occurring before that date *are exempt* from these taxes. Special reporting requirements are imposed for transfers where the position is taken that such a transfer is not taxable.

Extension of IDB authority to the District of Columbia and certain territories.—The conference agreement authorizes American Samoa and the Virgin Islands to issue tax-exempt IDBs, subject to the restrictions of the Code. Additionally, the District of Columbia is authorized to issue IDBs for multifamily residential rental property and mortgage subsidy bonds. (This rule reverses the effect of the *Chadha* decision insofar as it affects the ability of the District of Columbia to issue those bonds.) The $200 million minimum volume limitation does not apply in the case of American Samoa or the Virgin Islands. This provision sunsets after three years.

11. Prohibition on use of tax-exempt bonds for consumer loans

The conference agreement generally prohibits the use of tax-exempt bonds to provide consumer loans, effective for bonds issued after the date of enactment.

D. Miscellaneous Tax-Exempt Bond Provisions

The conference agreement provides that the Pennsylvania State University is to be treated as a State governmental unit for purposes of issuing tax-exempt bonds. The public approval requirement of present law is clarified as it applies to certain airports. The Power Authority of the State of New York is authorized to issued tax-exempt bonds, subject to the applicable volume limitation, for certain projects; certain other utilities are authorized to issue tax-exempt IDBs; and, certain issues for specific projects are exempted from various requirements of the law. Finally, certain clarifications of the rules governing tax-exempt student loan bonds are provided.

VII. TECHNICAL CORRECTIONS

This title contains technical, clerical, conforming and clarifying amendments to provisions enacted by the Tax Equity and Fiscal Responsibility Act of 1982, the Subchapter S Revision Act of 1982, the Highway Revenue Act of 1982, and other recently enacted tax legislation.

VIII. HIGHWAY REVENUE PROVISIONS

1. Heavy vehicle use tax and diesel fuel tax

Use tax

Under present law, the highway use tax is scheduled to increase on July 1, 1984, starting at $50 for vehicles of 33,000 pounds and reaching a maximum of $1,600 ($1,900 by July 1, 1988) for vehicles over 79,000 pounds.

The conference agreement restructures and reduces the use tax, so that it starts at $100 for vehicles of 55,000 pounds and reaches a maximum of $550 for vehicles over 75,000 pounds. Rules applicable to small owner-operators are amended. The tax rate on certain vehicles registered to haul harvested forested products is reduced by one-quarter the rate otherwise applicable. The present law exemption generally allowed for vehicles traveling fewer than 5,000 miles is increased to 7,500 miles in the case of agricultural vehicles used for farming purposes. These provisions of the conference agreement are effective on July 1, 1984.

In addition, the conference agreement requires the Secretary of Transportation to study the use tax, as it relates to the heaviest vehicles and to trans-border trucking, and the feasibility of weight-distance taxes and to report to Congress before October 2, 1987.

Diesel fuel tax

Under present law, an excise tax of 9 cents a gallon is imposed on the sale of diesel fuel for use in a highway vehicle. A refund or credit is allowed for tax paid on diesel fuel used in an intercity, local or school bus.

The conference agreement increases this tax by 6 cents a gallon (the diesel differential) to 15 cents a gallon. A fixed rebate, generally claimed one time on income tax forms, is allowed for the estimated diesel differential to be paid over the expected life of new or recent model-year, diesel-powered vehicles of 10,000 pounds or less. The conference agreement increases the credit or refund of tax paid on diesel fuel (not otherwise exempt because, e.g., purchased by a State or local government or non-profit educational organization for its exclusive use) used in an intercity, local or school bus to 12 cents a gallon (15 cents, if a local bus is operated for a State or local government), generally resulting in a 3-cents-a-gallon tax. These provisions are effective on August 1, 1984.

2. One-year extension of refund of taxes on fuels used in certain taxicabs

The conference agreement extends for one year, through September 30, 1985, the present rule permitting a 4-cents-per-gallon refund or credit with respect to Federal excise taxes paid on fuels used in certain taxicabs. The conference agreement further requires a Treasury Department study of the effectiveness of this exemption, to be submitted to Congress not later than January 1, 1985.

3. Modification of excise tax exemption for alcohol fuels mixtures and alcohol fuels; alcohol fuels credits; and duty on imported alcohol fuels

The conference agreement increases the present 5-cents-per-gallon excise tax exemption for alcohol fuels mixtures (e.g., gasohol) to 6 cents per gallon. The alcohol fuels credit and the duty on imported alcohol fuels are correspondingly increased to 60 cents per gallon from their present level of 50 cents per gallon. These provisions are effective on January 1, 1985.

The conference agreement reduces the tax rate from 9 cents to 4.5 cents a gallon for alcohol fuels (e.g., methanol) that are at least 85 percent pure and are comprised of alcohol derived from natural gas. This provision is effective on August 1, 1984.

4. Temporary reduction in excise tax on piggyback trailers

Present law imposes a 12-percent excise tax on the first retail sale of heavy truck trailers, including piggyback trailers. The conference agreement reduces this tax to 6-percent only for piggyback trailers sold within the one-year period beginning on the date of enactment, after which the tax rate on such trailers returns to 12 percent. The Secretary of Transportation is required to report to Congress before May 2, 1985, on this excise tax as it relates to piggyback trailers.

IX. MISCELLANEOUS REVENUE PROVISIONS

A. Estate and Gift Tax Provisions

1. Qualification of certain holding company stock for installment payment of estate tax

Under present law, estate tax attributable to interests in certain closely held businesses may be paid in installments extending up to 14 years, with principal payments being deferred for up to 5 years of that time. Additionally, a special 4-percent interest rate is available for certain amounts of deferred tax. Generally, only directly owned interests in active business operations are eligible for this benefit.

The bill permits executors to elect to consider the value of indirectly owned non-readily tradeable stock in an active business for certain purposes under the installment payment provision if the business interest would qualify were it owned directly. If this election is made, the 4-percent interest rate and 5-year deferral of principal payments are not available.

The bill further provides that investment assets held by any business are to be disregarded for all purposes under the installment payment provision. This rule is consistent with the present-law rule for valuing businesses carried on as proprietorships.

These provisions are effective for estates of individuals dying after the date of enactment.

2. Clarification that certain usufruct interests qualify for estate tax marital deduction

The Economic Recovery Tax Act of 1981 permitted executors to elect to claim an estate marital deduction for the value of certain qualifying income interests for life (so-called "QTIP" property). An income interest qualifies as QTIP property only if the surviving spouse is entitled to all income from the interest (payable at least annually) and no person has a power to appoint the property to any person other than the surviving spouse (except for powers exercisable only at or after the spouse's death).

The conference agreement clarifies that certain usufructs for life under the Louisiana Civil Code may qualify as QTIP property, if certain requirements are satisfied.

This provision is effective as if included in the Economic Recovery Tax Act.

3. Special estate tax credits for the Estate of Nell J. Redfield and the Estate of Elizabeth Schultz Rabe

The conference agreement provides a special credit against Federal estate tax for the estates of Nell J. Redfield and Elizabeth Schultz Rabe. The credit will apply to the transfer to the Secretary of Agriculture, within 90 days after enactment, of certain real property located within or adjacent to the Toiyabe National Forest that is included in the two estates. The amount of the credit will be equal to the lesser of the fair market value of the property on the date it is transferred or the transferor estate's Federal estate tax liability (plus interest).

4. Perfection of estate tax current use valuation elections

The conference agreement permits perfection of estate tax current use valuation elections by estates when the elections, as originally filed, substantially complied with the requirements of the Treasury regulations. This provision applies to estates of individuals dying after 1976.

5. No gain recognized from net gifts made before March 4, 1981

Present law taxes income "from whatever source derived," including the benefit resulting from the discharge of one's indebtedness by another party. Present law also imposes a gift tax on certain transfers for less than adequate consideration. Liability for the gift tax is on the donor of the transferred property.

A donor may transfer property pursuant to an agreement with the donee that the donee will pay any gift tax arising from the transfer (i.e., make a "net gift"). On June 15, 1982, the U.S. Supreme Court ruled in *Diedrich* v. *Commissioner*, that the discharge of a donor's liability for gift tax by the donee of a net gift gives rise to income to the donor to the extent that the gift taxes exceeded the donor's adjusted basis in the transferred property.

The conference agreement provides that no income will be recognized to donors who made net gifts before March 4, 1981 (the date on which an initial decision by the Court of Appeals held that the donor in the *Diedrich* case recognized gain).

6. Permanent rules for reforming governing instruments creating charitable remainder trusts and other charitable interests

Under the rules adopted by the Tax Reform Act of 1969, a charitable interest in a split-interest trust (i.e., a trust which is part charitable and part noncharitable) must be in certain specified forms to be deductible for Federal income, gift, and estate tax purposes. Present law permits defective governing instruments of charitable split-interest trusts which were created pursuant to wills executed before January 1, 1979, to be amended to conform to the 1969 Act rules by December 31, 1981.

The conference agreement permits governing instruments of charitable split-interest trusts which do not meet the requirements of the 1969 Act rules to be reformed where (1) the instruments evidence an intent to comply with the 1969 Act rules (or the reformation begins within a specified period), and (2) the actuarial values and durations of the charitable and noncharitable interests in the trust generally remain the same before and after the reformation.

This provision generally will be effective with respect to reformations made after December 31, 1978.

7. *Alternate valuation date election*

Under present law, the value of property includible in the decedent's gross estate for Federal estate tax purposes generally is determined on the date of the individual's death. However, the executor of the individual's estate may elect to have the value of all property included in the gross estate determined as of the alternate valuation date (which generally is six months after the individual's death). The election to use the alternate valuation date may be made only on a timely filed Federal estate tax return. Also, under present law, the Federal income tax basis of property acquired from a decedent generally is its value for Federal estate tax purposes.

The conference agreement provides that the election to use the alternate valuation date may be made only where both the total value of all property in the gross estate and the Federal estate tax liability of the estate are reduced by making the election. The conference agreement also allows the alternate valuation election to be made on the first estate tax return filed (whether filed timely or late), provided the return is filed no more than one year after the due date.

This provision is effective with respect to estates of individuals dying after the date of enactment. The provision also applies to estates of individuals dying before the date of enactment that would qualify under the amended alternate valuation date provision had the individuals died after the date of enactment.

B. Excise Tax Provisions

1. *Excise tax on sport fishing equipment*

The conference agreement expands the present manufacturers excise tax on fishing equipment. Certain additional articles and accessories are subject to the expanded tax at the present-law 10-percent rate and others (i.e., certain fishfinders and electric outboard motors) at a 3-percent rate. The conference agreement also extends the time for payment of the tax, with payments to be required on a quarterly basis.

Further, the conference agreement alters the financing sources and expenditure purposes for the existing sport fish restoration and boating safety programs and the financing sources for the Land and Water Conservation Fund. Among these changes, the conference agreement transfers part of the revenues from the existing tax on motorboat fuels (the excess each year over the $1 million to the Land and Water Conservation Fund and the up to $45 million per year, through fiscal year 1988, to the boating safety program) to the sport fish restoration program, as well as the revenues from import duties on sport fishing equipment and yachts and pleasure craft. The conference agreement also transfers administration of funding for the sport fish restoration and boating safety programs to a new Aquatic Resources Trust Fund, to be included in the Internal Revenue Code.

These provisions are effective on October 1, 1984.

2. *Excise tax on certain arrows*

The conference agreement expands the existing 11-percent excise tax on arrows to include arrows used by crossbow hunters, effective on October 1, 1984.

3. *Exemption from aviation excise taxes for certain helicopter operations*

The present exemption from the airways fuels and passenger ticket taxes for helicopters engaged in timber operations or hard mineral exploration and not using the Federally aided airport or Federal airways control systems are extended by the bill to helicopters engaged in oil and gas exploration, effective on April 1, 1984.

4. *Technical amendments to the Hazardous Substance Response Revenue Act of 1980*

Present law imposes an excise tax on certain chemical substances, the revenue from which go into the Hazardous Substance Response Trust Fund. The bill makes technical modifications to this excise tax in three areas. First, an exemption is provided for light hydrocarbons used in the production of motor fuels. Second, certain copper, lead, or zinc compounds which have a transitory existence during metal refining are exempted from tax. Third, the administrative mechanism through which the exemption for fertilizer may be claimed is simplified.

C. Income Tax Credits

1. *Changes in earned income credit*

Under present law, eligible taxpayers, i.e., individuals or couples with children, are allowed a refundable tax credit equal to 10 percent of the first $5,000 of earned income, for a maximum credit of $500. The maximum credit is phased down to zero as income increases from $6,000 to $10,000. The conference agreement increases the rate of the earned income credit to 11 percent, thereby increasing the maximum credit to $550. The conference agreement also raises the income range over which the credit is phased-out to the $6,500 to $11,000 range. These changes in the earned income credit will apply to taxable years beginning after 1984.

2. *Modification of rules governing rehabilitation investment credit*

The conference agreement provides an alternative to the present requirement that at least 75 percent of a building's external walls be retained as external walls in the case of rehabilitations with respect to which a rehabilitation credit is allowable. Under the alternative, the external walls test is deemed met if (1) at least 50 percent of the building's external walls are retained as external walls; (2) at least 75 percent of the building's external walls are retained as either internal or external walls; and (3) at least 75 percent of the building's internal structural framework is retained.

This provision is effective for rehabilitation expenditures incurred with respect to property placed in service after December 31, 1983.

3. Extension of targeted jobs credit

Under present law, the targeted jobs credit is available with respect to individuals who begin work for the employer before 1985. The conference agreement extends the targeted jobs credit for one additional year. Under the conference agreement, the credit will be available with respect to any member of a targeted group who begins work for the employer before 1986.

D. Six-Month Long-Term Capital Gain Holding Period and Reduction of Capital Loss Offset Against Ordinary Income

Under present law, gains and losses from the sale or exchange of capital assets held for more than 1 year are long-term capital gain or loss and gains and losses from capital assets held for 1 year or less are short-term.

The conference agreement reduces the long-term capital gain and loss holding period to 6 months for assets acquired after June 22, 1984, and before January 1, 1988. The special carryover treatment for long-term losses realized prior to 1970 is repealed, effective after 1986.

E. Miscellaneous Housing Provisions

1. Disaster loss deduction where taxpayer ordered to demolish or relocate residence in disaster area because of disaster

Present law allows a deduction for nonbusiness casualty loses to the extent such losses exceed $100 per loss and 10 percent of adjusted gross income for the taxable year. In general, a deduction is allowed only when the casualty (e.g., storm, flood or earthquake) causes actual physical damage to the taxpayer's property.

The conference agreement provides that certain taxpayers whose residences are located in a Federally declared disaster area, and who are ordered by a State or local government to demolish or relocate their residences, may deduct any loss attributable to the disaster as a casualty loss. The provision applies to taxpayers whose residences have been rendered unsafe for use as a residence as a proximate result of the disaster.

This provision applies to taxable years beginning after December 31, 1981, with respect to areas determined after that date to warrant Federal disaster assistance.

2. Housing allowance for ministers

In 1983, the IRS ruled that ministers may not take deductions for mortgage interest and real estate taxes on their residence to the extent that such expenditures are allocable to tax-free housing allowances provided for ministers. The new deduction disallowance rule generally applied beginning July 1, 1983. Under a transitional rule, in the case of a minister who owned and occupied a home before January 3, 1983 (or had a contract to purchase a home before that date), the deduction disallowance rule generally will not apply until January 1, 1985. The conference agreement extends this transitional rule date to January 1, 1986.

3. *Rollover of gain on sale of residence for military personnel stationed overseas*

Under present law, no gain is recognized on sale of a personal residence to the extent that the amount of the sales price of the old residence is reinvested in a new residence within a specified period of time. This period is suspended for up to four years where the taxpayer serves on extended active duty with the Armed Forces (sec. 1034(h)).

The conference agreement provides that, in the case of a member of the Armed Forces who is stationed outside the United States or who is required to reside in government quarters, the normal nonrecognition period will not expire until the end of four years after the sale of the old principal residence or one year after the member is no longer stationed outside the United States or no longer required to reside in government quarters, whichever is later, but not to exceed eight years. This provision applies to sales of residences occurring after the date of enactment.

4. *Home won as prize and designed for handicapped foster child of the taxpayer*

The conference agreement provides that no interest or penalties will be payable on the Federal income tax liability attributable to receipt of a residence won as a prize, and specially designed for a handicapped foster child of the taxpayer, where certain conditions apply, but only if the tax liability is paid no later than one year after the date of enactment.

F. Miscellaneous Extensions

1. *Transitional rule for treatment of certain income from S corporations*

The conference agreement provides an election for 1983 and 1984 to characterize income from an S corporation, for purposes of section 163(d), under the law in effect prior to the enactment of the Subchapter S Revision Act of 1982.

2. *Extension of PIK rules to 1984 wheat program*

Present law provides special tax treatment for commodities received by a producer under a 1983 PIK program for withdrawing land from production. Under these rules, producers may defer recognition of income on PIK commodities until the commodities are sold; PIK participants are not disqualified from various special tax provisions available to taxpayers engaged in the business of farming; and the applicability of income, employment, and estate tax provisions is not affected solely as a result of a taxpayer's participation in the PIK program. The conference agreement generally extends these special PIK tax rules to the 1984 wheat program.

3. *Special leasing rules for certain coal gasification facilities*

Under present law, safe-harbor leasing rules are generally not applicable to agreements entered into after December 31, 1983. Under the conference agreement, those rules, as in effect prior to TEFRA, are applicable to certain coal gasification facilities.

4. *Treatment of Indian tribal governments as State governments for tax purposes*

The conference agreement makes permanent the present treatment of Indian tribal governments as State governments for most purposes of the Internal Revenue Code, and adds certain additional purposes for which that treatment is available. As under present law, tribal governments will continue to be barred from issuing tax-exempt bonds, other than bonds to finance traditional government functions.

5. *Amortization of expenditures to rehabilitate low-income rental housing*

The conference agreement reenacts for three years, through December 31, 1986, the provision of prior law that permitted amortization over 60 months of certain rehabilitation expenditures incurred with respect to low-income housing.

6. *Reenactment of denial of deductions for costs of demolishing certified historic structures*

The conference agreement reenacts and expands the provision of prior law that denied income tax deductions for costs associated with demolition of certified historic structures. The expanded provision applies to demolitions of all buildings. This provision is effective on January 1, 1984.

7. *Architectural barrier removal expenses*

The conference agreement provides a deduction for up to $35,000 per year of expenses incurred in eliminating architectural and transportation barriers to the handicapped and elderly, effective for taxable years beginning in 1984 and 1985. This provision is similar to an expired provision of prior law.

G. Additional Provisions

1. *Tip reporting*

Under present law, if a large employer, for tip reporting purposes, demonstrates to the Secretary that the actual tip rate of his establishment is less than 8 percent, the Secretary may lower the percentage allocated (but not to less than 5 percent). The conference agreement allows employers or a majority of their employees to petition the Secretary for permission to allocate based on a tip rate as low as 2 percent and requires the IRS to provide rules for recordkeeping with respect to tips within a year.

2. *FUTA treatment of tips*

Under present law, tip income is considered wages for purposes of the Federal Unemployment Tax Act (FUTA) only to the extent paid directly to the employee by the patron, reported by the employee to the employer, and used by the employer to satisfy the minimum wage requirement of the Fair Labor Standards Act.

The conference agreement provides that all tip income reported by the employee to the employer is considered wages for FUTA purposes. The provision generally is effective on January 1, 1986.

However, in the case of any State the legislature of which (1) did not meet in a regular session which begins during 1984 and after the date of enactment, and (2) did not meet in a session which began on the date of enactment and remained in session for at least 25 calendar days after the date of enactment, the provision is effective on January 1, 1987.

3. FUTA exemption for certain fishing boat crew members

Remuneration paid to fishing boat crew members generally is subject to tax under the Federal Unemployment Tax Act (FUTA) if the services performed are related to catching halibut or salmon for commercial purposes or if the services are performed on a vessel of more than ten net tons. However, under a provision which expired on December 31, 1982, remuneration paid to fishing boat crew members was exempt from FUTA if the crew members are treated as self-employed for social security tax purposes and the remuneration of whom is exempt from the Federal Insurance Contributions Act (FICA) tax and income tax withholding. Fishing boat crew members are so treated if their remuneration depends on the boat's catch and the crew normally consists of fewer than ten members.

The conference agreement extends through December 31, 1985, the exemption from FUTA tax for remuneration paid to fishing boat crew members who are treated as self-employed for purposes of social security taxes.

4. Unemployment compensation for pre-1978 periods

The bill amends the Revenue Act of 1978 to provide that the provisions of that statute that make includible in income a portion of unemployment compensation benefits are to apply to payments of unemployment compensation made after 1978, except payments for weeks of unemployment ending before December 1, 1978. The bill also extends until one year after enactment the period for claiming any credit or refund attributable to this amendment.

5. Tax exemption for the National Credit Union Central Liquidity Facility

Under present law, the National Credit Union Central Liquidity facility ("Central Liquidity Facility") is not explicitly exempt from Federal, State or local taxes.

The conference agreement provides that the Central Liquidity Facility is exempt from Federal income taxes under the Internal Revenue Code, and from State or local taxes (other than real property taxes). Notes, bonds, and other obligations of the Central Liquidity Facility are to be exempt from State and local taxes (other than gift, estate, or other wealth transfer taxes), but will be subject to Federal tax.

These provisions are effective on and after October 1, 1979, i.e., the effective date of the legislation creating the Central Liquidity Facility.

6. Requirement that certain future tax exemptions be provided in the Internal Revenue Code

Under present law (sec. 501(c)(1), instrumentalities of the United States are tax-exempt if the tax exemption is specified in the Congressional act under which the instrumentality is organized.

The conference agreement provides that, effective on the date of enactment, further tax exemptions for United States instrumentalities must be specified in the Internal Revenue Code or in a revenue act. Instrumentalities of the United States will remain tax exempt if the exemption is provided in an act of Congress (i.e., non-Code provisions) as amended and supplemented before the date of enactment of the conference agreement.

7. Exclusion from gross income for cancellation of certain student loans

Under a provision in the 1976 Tax Reform Act, and later extended through 1982, an individual does not realize gross income from cancellation of student loans made by government agencies where the individual in return works for a certain period of time in certain professions in certain geographical areas or for certain classes of employers. The conference agreement provides a permanent exclusion from income for amounts realized by reason of cancellation of certain student loans where the recipient performs certain professional services for any of a broad class of employers, effective for debt cancellations occurring after 1982.

8. Migratory bird hunting and conservation stamps ("Duck Stamps")

Under the conference agreement, the Secretary of the Interior is authorized to allow reproductions in color, and black and white, of migratory bird hunting stamps for commercial purposes. Revenues will be deposited in the Migratory Bird Conservation Fund and will be used to help finance the purchase of additional wetlands acreage to be included in the National Wildlife Refuge. Color reproductions of duck stamps in philatelic (or stamp-collecting) advertising is permitted to encourage collectors to purchase duck stamps. Anticounterfeiting rules continue to apply, but licensing requirements will not apply.

9. Tax treatment of grants related to Boundary Water Canoe Area

The conference agreement allows tax-free reinvestment before 1986 of federal assistance grants made to resort operators and motorboat franchisors whose business activities had to be modified to conform to new statutory limits following conversion of their operating areas to the Boundary Waters Canoe Area Wilderness under the jurisdiction of the Forest Service.

10. Taxation of regulated investment companies

a. Personal holding companies permitted to qualify

Under present law, a regulated investment company (RIC) is treated, in essence, as a conduit for tax purposes. If a corporation is a RIC, it is allowed a deduction for dividends paid to its shareholders. One of the requirements that a corporation must meet in order to be a RIC is that it cannot be a personal holding company (PHC).

The conference agreement modifies the definition of a RIC to permit a PHC to qualify as a RIC. In the case of a RIC which is a PHC, any undistributed investment company taxable income of the RIC will be taxed at the highest corporate rate. The conference agreement also denies RIC status to companies first becoming a RIC after 1982 if the company has earnings and profits accumulated as a non-RIC.

The provision is effective for taxable years beginning after December 31, 1982. However, a corporation with earnings attributable to a non-RIC year will be eligible to elect RIC status without distributing such earnings if it completed all the economic steps required to elect RIC status during the period beginning on January 1, 1982, and ending on November 7, 1983, and elects RIC status for its first taxable year beginning after November 7, 1983.

b. Timing of income from short-term government securities

Under present law, discount income on short-term government securities is includible in income at the earlier of the date of maturity or the date of sale.

The bill would allow a RIC to elect to include discount income on short-term government securities as it accrues. This provision is effective for taxable years beginning after 1978.

H. Studies

1. Study of alternative tax systems

The conference agreement instructs the Secretary of the Treasury to conduct a study covering the advisability of developing an alternative tax system that would reduce the complexity of the present income tax system and improve the efficiency and equity of the tax system. Alternative tax systems that should be evaluated include a simplified income tax based on gross income, a consumption-based tax restructuring and broadening of the current income tax base combined with lowering of current tax rates, a national sales tax, and a value-added tax. The study is to be submitted by December 31, 1984, and is to include a study of tax shelters.

2. Treasury study of foreign taxation of certain U.S. services

Under present law, taxpayers who perform services in the United States for use in foreign countries are subject to full U.S. tax on their income from those services. The foreign country where the services are used may also subject the income from those services to tax. The conference agreement directs the Treasury Department to study the practices of foreign countries that impose taxes on the basis of services that are performed in the United States, including the status of treaty negotiations with such countries, and options to alleviate the resulting double tax burden on U.S. taxpayers. The Treasury Department is to report on the results of its study no later than December 31, 1984.

PART TWO: SUMMARY OF SPENDING PROVISIONS WITHIN THE JURISDICTION OF THE COMMITTEE ON WAYS AND MEANS AND THE COMMITTEE ON FINANCE

TITLE VI—OASDI, SSI, AFDC AND OTHER PROGRAMS

A. Improvements in OASDI Program

1. Social security treatment of certain church employees

Under the Social Security Amendments of 1983, employees of religious and other nonprofit organizations (not including ministers or members of religious orders) are subject to mandatory social security coverage, effective January 1, 1984. Prior to these amendments, employees of nonprofit organizations were exempt from social security coverage unless the organization waived, or was deemed to waive, its exemption.

The conference agreement provides a one-time irrevocable election by a church or qualifying church-controlled organization to exclude from the FICA tax base remuneration for all services performed for the organization, other than in an unrelated trade or business. The employees of organizations so electing are liable for self-employment (SECA) taxes with respect to the excluded services.

For employees of electing organizations, wages of less than $100 per calendar year are not subject to SECA taxes and the SECA tax base is generally conformed to the applicable FICA rules.

Electing organizations remain subject to income tax withholding and reporting requirements with respect to all employees. Treasury may revoke an election for continuing failure to provide required information.

An election is available to: (1) churches (including conventions or associations of churches), (2) elementary or secondary schools controlled, operated, or principally supported by churches (or conventions or associations of churches), and (3) church-controlled tax-exempt organizations (sec. 501(c)(3)), except any such organization which both—

> (A) offers goods, services, or facilities for sale to the general public (e.g., to persons who are not church members), other than on an incidental basis and other than at a nominal charge, and also
>
> (B) normally receives more than 25 percent of its support from the sum of (a) governmental sources, and (b) receipts from admissions, sales of merchandise, performance of services or furnishing of facilities other than in unrelated trades or businesses.

To make an election, an organization must state that it is opposed for religious reasons to payment of social security taxes.

2. *Coverage of employees under social security and Federal retirement systems*

a. Breaks in service

The Social Security Amendments of 1983 provided social security coverage for newly hired Federal civilian employees effective with remuneration paid after December 31, 1983. Persons continuously in the employ of the United States since December 31, 1983 (or with a break in such employment of 365 days or less) will not be covered. Legislative branch employees are covered by social security unless they were covered by the Civil Service Retirement System (CSRS) on December 31, 1983.

Contrary to the intent of Public Law 98-21, a person in Federal employment that is already covered by social security, (mainly the armed services, which have been covered since 1956) can retire from military service, enter Federal civilian service, and be exempt from social security as long as the break between military and civilian service does not exceed 365 days. Conversely, a person who only technically severs his Federal civilian employment connection in order to serve a term of duty with an international organization would be treated as having had a break in service upon his return to domestic service, and would be covered under social security if such break exceeded 365 days.

In order to prevent Federal employees who had been previously covered under social security from losing coverage as a result of a break in service of less than 365 days, the conference agreement provides that persons transferring from government service that was covered under Social Security prior to January 1, 1984 to civilian service newly covered by P.L. 98-21 will be covered under social security, unless the person is returning to civilian service after temporary military or reserve duty and is exercising reemployment rights under chapter 43 of title 38, U.S.C.

The conference agreement also continues the exemption from social security coverage for Federal employees who have a break in service of more than 365 days to the extent that the break in service results from service in an international organization or the American Institute in Taiwan.

b. Legislative branch employees

Legislative branch employees who were covered by CSRS on December 31, 1983, can withdraw from CSRS after that date and not be covered by social security or CSRS.

The conference agreement provides that any legislative branch or other Federal employee who withdraws from CSRS after June 14, 1984 and takes a refund of his contributions may not thereafter be exempt from social security coverage while employed in the legislative branch. In addition, an individual who has any legislative branch employment after June 14, 1984 which is not subject to CSRS could not also be exempt from social security coverage (regardless of whether he has applied for a refund of his prior CSRS contributions.) Employees in the legislative branch who take leaves of absence without taking a refund of their CSRS contributions may (according to the practice of the employing office) continue to be covered under CSRS. If they are not automatically re-covered under CSRS, they will be covered under social security unless they re-join CSRS upon resumption of their legislative branch employment.

Under the conference agreement, the exemption for social security coverage will also cease to be available to any individual who took a refund of CSRS contributions based on a separation or transfer during the period from January 1, 1984 through June 14, 1984 or who has legislative branch employment which was not covered under CSRS during that period. However, any such individual can reestablish the exemption (provided that he was covered under CSRS or another Federal retirement system on December 31, 1983) if he has reentered CSRS after the point when he last withdrew from it and prior to the 31st day after enactment. For an individual who is not in Federal employment on the date of enactment, the 30 day period will run from the date on which he again becomes a legislative branch employee. An individual will be considered to have reentered CSRS if he applies to do so within the appropriate time and the coverage subsequently does become effective.

c. Nonprofit organizations

Effective January 1, 1984, employees of all nonprofit organizations are covered by social security on a mandatory basis. Employees in certain nonprofit organizations (Legal Services Corporations, for example) who are covered on a mandatory basis by the Civil Service Retirement System (CSRS) are thus covered on a mandatory basis by social security as well. These employees are not provided relief from double-taxation under Title II of the Federal Physicians Comparability Allowance Amendments of 1983 (Public Law 98-168), known as the Federal Employees' Retirement Contribution Temporary Adjustment Act.

The conference agreement provides that employees of nonprofit organizations who are covered on a mandatory basis by CSRS would be treated like Federal employees for purposes of social security. They would therefore be covered by social security only if newly hired after January 1, 1984, or if they had a break in Federal service lasting more than 365 days. In such cases, the provisions of P.L. 98-168 would apply to them. This provision would apply to services performed on or after January 1, 1984.

3. Increased enforcement of earnings test

Under present law, social security beneficiaries are not required to file earnings reports until the close of the calendar year.

The conference agreement requires the Secretary to implement procedures for obtaining earnings reports earlier than under present law and to make earlier adjustments of benefit amounts on account of excess earnings.

B. AFDC and SSI Programs

Aid to Families with Dependent Children (AFDC) Provisions

1. Gross income limitation

Under present law, eligibility for AFDC is limited to families with gross incomes at or below 150 percent of the State standard of need. The conference agreement increases the gross income limitation to 185 percent of the State standard of need.

2. Work expense deduction

Under present law, States are required to disregard the first $75 of monthly earnings for full-time work expenses; a lower deduction must be established for part-time workers. The conference agreement requires States to disregard the first $75 monthly for full and part-time workers.

3. Continuation of $30 disregard

Under present law, the $30 plus one-third of remaining earnings disregard is limited to four months. The conference agreement retains the four month limit on the one-third disregard but extends the $30 disregard for an additional eight months for a total of twelve months.

4. Work transition status

Under present law, a family who loses AFDC eligibility due to the four month limit on the earnings disregard, simultaneously loses categorical eligibility for Medicaid. The conference agreement provides that families who lose AFDC because of the termination of the earnings disregard will be eligible for nine months of Medicaid coverage. At State option, an additional six months of Medicaid coverage can be provided. In addition, families who lost AFDC eligibility prior to enactment of the work transition will also be eligible for Medicaid under certain specified circumstances.

5. Clarification of earned income provisions

The conference agreement clarifies that the term "earned income" as used in the AFDC program means the gross amount of earnings, prior to the taking of payroll or other deductions.

6. Burial plots, funeral agreements and certain property

Under present law, burial plots and funeral agreements are counted toward the $1,000 asset limit. The conference agreement exempts from the AFDC resource limitation, burial plots and funeral agreements. An AFDC policy on real property that is similar to SSI policy is also established.

7. Federal matching for Community Work Experience Program (CWEP) expenses

Under present law, States must reimburse a CWEP participant for necessary transportation and other expenses. Federal matching for this reimbursement is, by regulation, limited to $25 per month. The conference agreement requires States to reimburse a CWEP participant for costs incurred if the State is unable to provide directly any transportation or day care services. Reimbursement of day care expenses is limited to those determined by the State to be reasonable, necessary and cost effective up to $160 per month per child.

8. Retrospective budgeting and monthly reporting

Under present law, monthly reporting and retrospective budgeting are required for all AFDC cases; however, the Secretary of Health and Human Services may waive the monthly reporting requirement if it is not cost effective to require the report. The conference agreement mandates retrospective budgeting for cases filing a monthly report. Monthly reporting is required when cost effective; cases with earned income and recent work history must report monthly.

9. Earned income tax credit (EITC)

Under present law, States must assume that an individual is receiving the earned income tax credit on an advance basis regardless of when or if it is received. The conference agreement requires States to count the EITC only when actually received.

10. Demonstrations of one-stop service delivery

The conference agreement authorizes from 3 to 5 Federally assisted demonstration projects designed to test the effectiveness and efficiency of integrating the delivery of human services.

11. Work requirements for pregnant women

The conference agreement adds to those who are exempt from work registration, any woman who is in the third trimester of pregnancy.

12. Recalculation of lump sum income

Under present law, States may only recalculate ineligibility due to receipt of lump sum income if a life threatening circumstance occurs. The conference agreement allows States to recalculate the ineligibility period under other specified circumstances. Ineligibility may be recalculated if: (1) an event occurs which would have changed the amount of AFDC paid; (2) the income becomes unavailable for reasons beyond the family's control; and/or (3) the family incurs, becomes responsible for and pays medical bills which offset the lump sum income.

13. Overpayment recoupment

Under present law, States must attempt to recover all benefit overpayments. The conference agreement permits States to waive overpayment recovery when it is not cost effective. States will be permitted to automatically waive overpayments of less than $35. Larger overpayments must be collected unless the State determines, after attempting to collect the overpayment, that the cost to collect would exceed the amount owed.

14. Protective payments

Under present law, States are required to make protective payments to a third party when a parent on AFDC fails to meet certain statutory procedural requirements. The conference agreement permits States to make the payment to the parent if, after all reasonable efforts have been made, a suitable protective payee cannot be found.

15. Eligibility requirements for aliens

Under present law, the income of an individual who sponsors a non-refugee alien is deemed to be available to the alien for three years after entry into the United States. The conference agreement establishes a similar policy for aliens who are sponsored by organizations or agencies.

16. Fugitive felons

The conference agreement permits States to disclose the current address of an AFDC recipient if a law enforcement agency provides the correct social security number and demonstrates that the recipient is a fugitive felon.

17. Payment schedule for back claims

The conference agreement establishes a payment schedule for court-ordered reimbursements and certain other back claims owed by the Federal government to the States that have been allowed or are pending.

18. Work supplementation program

The conference agreement modifies the existing work supplementation program to provide additional flexibility to States in operating grant diversion programs in which all or part of the AFDC grant can be used to subsidize a job.

19. Disregard of in-kind income

The conference agreement extends, until October 1, 1987, the disregard of certain in-kind assistance provided on the basis of need.

20. Standard filing unit/child support payments

There is no requirement in present law that parents and all siblings be included in the AFDC unit. The conference agreement requires States to include in the filing unit the parents and all minor siblings living with a dependent child who applies for or receives AFDC. In addition, a monthly disregard of $50 of child support received by a family is established.

21. CWEP work for Federal agencies

The conference agreement permits Federal agencies or offices to serve as community work experience program (CWEP) sites under the same requirements as apply to other sites.

22. Earned income of full-time students

For purposes of applying the gross income limitation, the conference agreement allows States to disregard the income of an AFDC child who is a full-time student.

Supplemental Security Income (SSI)

1. Increase in dollar limitations under SSI assets test

The conference agreement increases the countable assets limit under the SSI program by $100 a year for an individual and $150 a year for a couple, beginning in calendar year 1985, and each year through calendar year 1989. The current assets limit is $1,500 for an individual and $2,250 for a couple. The limit would be $2,000 for an individual and $3,000 for a couple in 1989 and thereafter.

2. Limitation recoupment rate in case of overpayments

The conference agreement establishes a limit on the rate of recovery from SSI recipients who have been overpaid. In the case of overpayments, the conference agreement limits the amount of adjustment or recovery in any month to the lesser of: (1) the amount of the benefit for that month; or (2) an amount equal to 10 percent of the countable income (including the SSI payment) of the individual (or couple) for that month. This limitation would not apply if there is fraud in connection with the overpayment. The recipient may request a different rate at which benefits or income may be withheld or recovered.

3. Limit on recovery of overpayments when recipient has excess assets

Under present law, if in any month, a recipient's assets exceed the asset limit (currently $1,500 for an individual and $2,250 for a couple) the individual is ineligible for benefits in that month and the entire amount of the benefit paid for that month is considered an overpayment subject to recovery. The conference agreement provides that in cases where there is an overpayment based on an excess of assets of $50 or less, the recipient would be deemed to be without fault for purposes of waiving the overpayment and the overpayment would not be recovered unless the Secretary finds that the failure to report the excess was knowing and willful on the part of the recipient.

4. Exclusion of retroactive payments from resources

Under present law, for purposes of determining SSI eligibility and benefit amounts, a retroactive SSI check is not counted as income to the recipient. By regulation, the Social Security Administration has provided that a retroactive SSI check is not counted as a resource for three months beyond the month in which it is received. A retroactive social security (title II) check is considered to be unearned income in determining the applicable monthly benefit amount, and is considered a resource if it is retained in months thereafter. The conference agreement provides that SSI and title II retroactive benefit payments may not be considered as a resource for a period of 6 months after the month in which the retroactive benefit is received.

5. Adjustments in SSI and OASDI benefits on account of retroactive payments

Under present law, OASDI benefits that are paid retroactively following the initial determination of eligibility are reduced by the amount of any excess SSI benefits that have been paid because the OASDI benefits have been received in a lump sum rather than in the months when regularly payable. The conference agreement would expand this provision to also provide for reducing the retroactive SSI payment in cases where retroactive OASDI benefits are paid before the SSI benefits and to make other technical changes.

6. Exclusion from income of Alaska bonus payment

An amendment to the SSI statute in 1975 provided for the exclusion from countable income of the Alaska "longevity bonus," i.e. payments to certain individuals who have lived in the State at least 25 years. As the result of an Alaska State Supreme Court decision, Alaska enacted a revision that reduces the residency requirement from 25 years to one year. The conference agreement provides for the continued disregard of the Alaska bonus but it would apply only to those individuals who, prior to October 1, 1985, meet the 25-year residency requirement of eligibility for the Alaska bonus as it was in effect prior to the recent amendments mandated by the courts.

C. Implementation of Grace Commission Recommendations

1. Income and eligibility verification procedures

Under present law, IRS wage information furnished by employers to IRS is available to state welfare agencies for use in their AFDC and food stamp programs, and to the Social Security Administration for administering the SSI program. However, IRS unearned income information (filed by a financial institution or corporation with respect to payments to individuals in the form of interest, dividends, etc.) is not available to Federal and State agencies for use in the administration of these programs. Quarterly wage information from the unemployment compensation program is available to State welfare agencies in most States.

The conference agreement provides for the IRS to disclose return information with respect to unearned income to Federal, State, or local agencies administering AFDC, SSI, Medicaid, food stamps, and the cash assistance programs administered in Puerto Rico, Guam, and the Virgin Islands.

Disclosure can only be made to agencies that meet the requirements to safeguard this confidential information against disclosure, and verification of the unearned income information is required prior to taking action to reduce or terminate benefits.

The provision also replaces existing statutory provisions relating to use (for purposes of AFDC) of return and other wage information and use of social security numbers, by adding a new section to the Social Security Act requiring States to have in effect an income and eligibility verification system for use in administering the AFDC, Medicaid, unemployment compensation, and food stamp programs (and the adult assistance programs in the territories). State agencies must request and make use of: (1) wage and other income information available under the Internal Revenue Code; and (2) quarterly wage information. Each State is required as of September 30, 1988, to maintain a quarterly wage reporting system, although not necessarily through its unemployment compensation system.

The income and eligibility system requires use of standardized data formats to facilitate exchange of information, for the purpose of identifying and reducing ineligibility and incorrect payments.

2. Collection and deposit of payments to executive agencies

Under present law, Federal agencies may collect nontax debt in a variety of ways. The Department of the Treasury collects a large proportion of nontax receipts through accelerated systems, including the Treasury Federal Communications System, automatic account withdrawals, and lockboxes. However, in 1983 $55 billion in nontax receipts was collected by means other than accelerated systems.

The conference agreement authorizes the Secretary of the Treasury to prescribe the mechanisms to be employed by Federal agencies to collect nontax debts and the timeframes for deposit of funds. The provision generally reduces from 30 days to three days the statutory period for timely deposit of funds by custodians, and requires that agencies adopt collection and deposit methods as prescribed by the Secretary.

3. Collection of nontax debts owed to Federal agencies

Present law does not provide authority for the IRS to offset tax refunds against nontax debts owed to Federal agencies. However, tax refunds must be offset against past-due child and spousal support payments in the case of families receiving AFDC payments.

The conference agreement provides that the amount of any IRS refund be reduced by the amount of certified nontax debt to the Federal government. Federal agencies must certify to the Secretary of the Treasury that specific attempts to notify the debtor have been made, and that the debtor does not dispute the debt, has not begun to repay the debt, and exhibits no reasonable intention to repay the debt. The agency must have entered into an agreement with the Secretary providing for the transmission of certified debt information before transmission occurs.

The provision authorizes the Secretary to test the offset procedures with selected programs before full implementation, and gives the Secretary authority to prescribe terms of agreements with other agencies and the format for transmitting information.

AFDC child support obligations would be subject to offset before other Federal debts. Beneficiary debts under the OASDI programs are excluded from this provision.

D. Technical Corrections

Subtitle D contains a number of minor technical amendments to the Social Security Act and the Internal Revenue Code, to correct clerical and other minor errors either resulting from the Social Security Amendments of 1983, or already existing in those acts. Most were contained in the House bill, and were accepted as part of the conference agreement.

The most significant of these amendments deals with that provision of the Social Security Amendments of 1983 which codified the

Rowan decision. The effective date of the provision of the Social Security Amendments of 1983 overriding the *Rowan* decision is clarified so that the provision applies for all purposes, other than the treatment of certain employer-provided meals and lodging, both to remuneration paid after March 4, 1983, and to remuneration paid on or before March 4, 1983, which the employer treated as wages when paid.

E. Trade Adjustment Assistance (Trade Act of 1974 Provisions)

1. Limitations on trade readjustment allowances

Under section 233(a)(3) of the Trade Act of 1974, the 26 weeks of additional trade readjustment allowances (TRA) that an eligible worker may receive while in training can be collected only during the 26 weeks immediately following exhaustion of entitlement to basic TRA.

The conference agreement amends section 233(a)(3) of the Trade Act of 1974 upon enactment to enable workers to collect the extra 26 weeks of TRA beginning with the first week the worker enters training if that training has not been approved until after the last week of entitlement to basic TRA benefits.

2. Job search and relocation allowances

Under sections 237 and 238 of the Trade Act of 1974, eligible workers can be reimbursed for 90 percent of necessary job search expenses up to a maximum of $600; relocation allowances consist of 90 percent of reasonable and necessary expenses, plus a lump sum payment of three times the worker's average weekly wage, up to a maximum of $600.

The conference agreement amends sections 237 and 238 of the Trade Act upon enactment to increase the maximum job search allowance to $800 and the maximum lump sum relocation allowance to $800.

3. Assistance to industry

Section 265 of the Trade Act of 1974 authorizes the provision of technical assistance programs for industries in which a substantial number of firms have been certified as eligible to apply for adjustment assistance. The section limits industry-wide technical assistance to improve competitiveness to $2 million annually per industry; only industries in which a substantial number of firms have been certified are eligible.

The conference agreement amends section 265 of the Trade Act upon enactment to extend eligibility also to industries in which a substantial number of workers have been certified eligible, and increases the maximum amount of annual assistance per industry to $10 million.

F. Provisions Relating to Puerto Rico and the Virgin Islands

1. Clarification of the definition of articles produced in Puerto Rico and the Virgin Islands

Federal excise tax revenues derived from articles coming into the United States from Puerto Rico or the Virgin Islands generally are paid to the Treasury of Puerto Rico or the Virgin Islands, respectively. Additionally, excise tax revenues derived from rum imported into the United States from any country are paid to Puerto Rico and the Virgin Islands.

Puerto Rico presently conducts a program under which grain neutral spirits, originally distilled in the United States, are transported to Puerto Rico, redistilled, and returned to the United States. Puerto Rico provides government subsidies to participants in this program to induce their participation in the program.

The conference agreement provides that payment of excise tax revenues will be made to Puerto Rico or the Virgin Islands with respect to articles containing distilled spirits which are brought into the United States from those possessions, only if at least 92 percent of the alcoholic content of the articles is rum. For articles other than distilled spirits, excise tax revenues generally will be paid to Puerto Rico or the Virgin Islands only if (1) in the case of any article brought into the U.S. from Puerto Rico, at least 50 percent of the value of the article is attributable to Puerto Rican input; and (2) in the case of any article brought into the U.S. from Puerto Rico or the Virgin Islands, only if no subsidy is provided for the production of the article which is of a kind different from (or in an amount per value or volume greater than) subsidies provided to industry generally.

Subject to limited payments with respect to redistilled spirits and cane neutral spirits, the provision is effective for articles brought into the U.S. after February 29, 1984.

2. Limitation on excise tax payments to Puerto Rico and the Virgin Islands with respect to distilled spirits

The conference agreement limits the amount of excise tax that may be paid to Puerto Rico or the Virgin Islands with respect to distilled spirits to a maximum of $10.50 per proof gallon (i.e., the present rate of tax). Therefore, the $2.00 per proof gallon increase in the excise tax on distilled spirits provided by the conference agreement will not be paid to Puerto Rico or the Virgin Islands with respect to distilled spirits brought into the U.S. from those possessions.

TITLE III—MEDICARE, MEDICAID AND MATERNAL AND CHILD HEALTH AMENDMENTS

Subtitle A—Medicare Amendments

1. Payment for costs of hospital-based mobile intensive care units (section 2320)

The conference agreement would provide that Medicare make payment to hospitals for a limited period of time under Part A for the operation of mobile intensive care units if certain conditions are met. The hospital must be located in New Jersey and operating under a demonstration project approved under Section 402 of the 1967 amendments.

2. Payment for the services of nurse anesthetists (section 2312)

The conference agreement would remove from the definition of "operating cost of inpatient hospital services", for purposes of prospective payment, costs related to services performed by CRNA's. Thus, such services will be reimbursed on a cost basis rather than under the prospective payment system. The provision would be effective for cost reporting periods beginning on or after October 1, 1984, and before October 1, 1987.

3. Prospective payment wage index (section 2316)

The conference agreement would require the Secretary, in consultation with the Secretary of Labor, to conduct a study to develop an appropriate index to adjust the prospective payment amounts to reflect area differences in average hospital wage levels, taking into account wage differences of full-time and part-time workers. The Secretary would be required to report the results of the study to Congress within 30 days of enactment.

The conference agreement would require the Secretary to adjust hospital payment amounts for cost reporting periods beginning on or after October 1, 1983, to reflect any changes in the wage index as a result of the study, but adjustments in the payment would not be made for the first such year until the succeeding cost reporting period.

The Secretary would be directed to conduct a study, and include in his final report, proposed criteria by which an adjustment could be made in a hospital's wage index if such index did not accurately reflect the hospital wage levels in the labor market area serving the hospital.

4. Skilled nursing facility reimbursement (section 2319)

The conference agreement would provide that, for cost reporting periods beginning on or after October 1, 1982 and prior to July 1, 1984, hospital-based facilities and free-standing skilled nursing facilities would be paid on the same basis used to calculate reimbursement limits that had been in effect prior to the passage of TEFRA.

In addition, the conference agreement would provide that for cost reporting periods beginning on or after July 1, 1984, separate limits would continue to be established for free-standing facilities in urban and rural areas at 112 percent of the mean operating costs of urban and rural free-standing facilities, respectively. Limits for urban or rural hospital-based facilities would be set at the appropriate free-standing facility limit plus 50 percent of the difference between free-standing facility limits and 112 percent of mean operating costs for hospital-based facilities.

The conference agreement would require the Secretary to submit to Congress, by August 1, 1984, the results of the study required by TEFRA relating to the development of legislative proposals for prospective reimbursement for SNF's. In addition, the Secretary would be required to report to Congress by December 1, 1984, on the range of options available for prospective payment of SNF's. Included in the study should be an examination of the feasibility, advisability and methods of incorporating into the hospital DRG system payment for SNF services. This examination should take into account case mix differences between providers.

5. Limitation on increase in hospital costs per case (section 2310)

The conference agreement would limit for the two hospital cost reporting periods beginning on or after October 1, 1984, the rate of increase applicable to hospitals. In fiscal year 1985, the rate of increase should be market basket plus one-quarter of one percentage point. However, budget neutrality would continue to apply in fiscal year 1985. In fiscal year 1986, the rate of increase may not exceed the market basket plus one-quarter of one percentage point. The Secretary, taking into account the recommendations of the Prospective Payment Assessment Commission, would continue to have authority to establish a rate of increase, as under current law, but not more than market basket plus one-quarter of one percentage point during the applicable period.

The conference agreement would provide that the rate of increase for exempted hospitals and exempted hospital units would not exceed market basket plus one-quarter of one percentage point in the first year or the second year.

6. Classification of certain rural hospitals (section 2311)

The conference agreement would provide the hospitals located in counties redesignated as rural since enactment of the prospective payment system would be allowed a two year transition to the rural rates. In the first year, the hospital would be paid the rural rates plus two-thirds of the difference between its rural and urban rate. In the second year, it would be paid the rural rate plus one-third the difference between the rural and the urban rates. The provision would be effective with respect to cost reporting periods beginning on or after October 1, 1983.

The conference agreement would specify that a hospital located in an MSA shall be deemed to be in the region in which the largest number of the hospitals are located or, at the option of the Secretary, the region which accounts for the majority of the Medicare discharges. The provision would be effective with respect to cost reporting periods beginning on or after October 1, 1983.

The conference agreement permits a rural hospital to appeal to the Secretary to be classified as a rural referral center, based on the similarity of its operating characteristics with those of a typical urban hospital in the same region. The provision would be effective for cost reporting periods beginning on or after October 1, 1984.

7. Prospective payment assessment commission (section 2313)

The conference agreement would clarify that the Commission is an independent body responsible for requesting appropriations. It would authorize an Executive Director and exempt the Commission from competitive public bidding. Open meeting requirements could be waived upon the affirmative vote of a majority of the Commission members. In addition, it would authorize the Secretary to supplement the Commission's activities by carrying out or awarding grants or contracts for original research and experimentation, including clinical research. It would provide that physicians serving as Commission personnel may be provided a physician comparability allowance.

8. Hospice contracting for core services (section 2343)

The conference agreement would permit the Secretary to waive the nursing care "core services" requirement for hospices which are located in rural areas, which were in operation on or before January 1, 1983, and which have demonstrated a good faith effort to hire their own nurses. A waiver request, containing information the Secretary may require, would be granted unless expressly denied by the Secretary. The granting of a waiver request would not preclude the favorable consideration of a subsequent waiver request should such a request be necessary.

The Secretary would be required to study the necessity and appropriateness of the "core services" requirement, including an analysis of Medicare certified hospices and a review of non-Medicare hospices, and report the findings to Congress, prior to January 1, 1986.

9. Payment for clinical diagnostic laboratory tests (section 2303)

The conference agreement would require the establishment of a fee schedule for all laboratory services except those provided to hospital inpatients.

A fee schedule for independent clinical labs (including hospital labs furnishing services to persons who are not patients of the hospital) and for lab tests performed in a physician's office is to be established at 60 percent of the prevailing charge levels for the fee screen year beginning July 1, 1984. After three years, payment would be made on the basis of a national fee schedule. (The fee schedule would not apply to clinical lab tests furnished by ESRD facilities and included in the ESRD composite rate.)

For hospital-based labs serving hospital outpatients, a fee schedule based on a carrier or regional area would be established at 62 percent of the prevailing charge levels for the fee screen year beginning July 1, 1984. After the three year period, reimbursement for such hospital labs would revert to cost reimbursement unless the Congress acted to include them in a national fee schedule.

The conference agreement would permit the Secretary to provide for adjustments for wage variations.

The conference agreement would require the Secretary to adjust the fee schedules annually to reflect changes in the Consumer Price Index for all Urban Consumers (U.S. city average).

The conference agreement would permit the Secretary to make adjustments or exceptions to the fee schedule to assure adequate reimbursement for: (a) emergency lab tests needed for the provision of bona fide emergency services; (b) certain low-volume, high-cost tests where highly sophisticated equipment or extremely skilled personnel are necessary to assure quality; and (c) technological changes.

In addition, the conference agreement would make the following changes:

(a) independent labs would be required to accept Medicare assignment;

(b) services conducted by hospital labs for non-hospital patients would have to be accepted on an assignment basis; and

(c) Medicare would waive the deductible and coinsurance requirements and pay 100 percent of the fee screen amount or charge, whichever is lower, for those cases which are accepted on assignment.

The conference agreement would permit physicians to bill for clinical lab services only if the physician (or another physician with whom the physician shares his practice) personally performed or supervised the performance of the test. As under current law, the physician could choose to accept or not accept assignment on a case by case basis. When a physician accepts assignment, Medicare reimbursement would be 100 percent of the fee screen amount, or charges, whichever is lower.

The conference agreement would provide that Federal matching funds would not be available to the extent that a State paid more for lab tests than would be paid for such tests under the Medicare fee schedule.

10. Coverage of administration of hepatitis B vaccine (section 2323)

The conference agreement would cover hepatitis B vaccine for Medicare beneficiaries at high and intermediate risk of contracting hepatitis B. It would authorize the Secretary to provide payments that reasonably reflect the cost of efficiently providing and administering hepatitis B vaccine.

11. Payment for services of teaching physicians (section 2307)

The conference agreement would revise the formula for calculating teaching physicians' customary charges. As a result, customary charges cannot be less than 85 percent of the Medicare prevailing charges paid for services in the same locality as the teaching setting.

As of October 1, 1984, if all the "teaching physicians" at a particular teaching hospital agree to take Medicare assignment for all Medicare patients they serve in that hospital then they can receive 90 percent of the Medicare prevailing charges in the same locality.

The Secretary would be directed, when calculating a hospital's indirect teaching cost, to take into account not only the interns and residents it employs but also any other house staff members who participate in the hospital's teaching program but who are employed by another organization.

12. Limitation on physician fee prevailing and customary charge levels; participating physician incentives (section 2306)

Under current law, Medicare pays for physician services on the basis of Medicare-determined "reasonable charges." Reasonable charges are the lesser of: (1) a physician's billed charge; (2) the customary charge made by an individual physician for a specific service; or (3) the prevailing level of charges made by all physicians for similar services in a geographic area. The customary and prevailing charges are updated annually (on July 1) to reflect changes in physicians' charging practices. Increases in the prevailing charge levels are limited by an economic index, which reflects changes in the physicians' practice costs and changes in general earnings levels.

The conference agreement provides for a 15-month physician reimbursement freeze under the Medicare program, protects Medicare beneficiaries from additional "extra-billing" and establishes a participating physician arrangement under the Medicare program.

a. Physician freeze

Customary and prevailing charges under the Medicare program would be frozen at the June 30, 1984 level for 15 months, until September 30, 1985. Subsequent fee screen updates would occur on October 1 of each year. Physicians would be expected not to increase their charges to Medicare beneficiaries during the 15-month freeze.

There would be no provision in the future fee screen updates for a "catch-up" in the prevailing charges. Any increases in the charges of nonparticipating physicians during the 15-month fee freeze period would not be recognized in future customary charge screen updates, as it is assumed that these physicians will not be increasing their charges to Medicare beneficiaries. Fee increases, if any, by participating physicians would be reflected in future customary charge updates (these physicians accept the Medicare reasonable charge as payment in full).

b. Participating physicians

Before October 1 of each year, physicians could elect to become participating physicians for the entire 12-month period beginning October 1. Participating physicians would agree, in writing, to accept the Medicare reasonable charge as payment in full, except for the allowed 20 percent coinsurance; that is, participating physicians would agree to accept Medicare assignment for all their Medicare patients. (Non-participating physicians could continue to accept assignment on a case-by-case basis.)

Additional incentives for physicians to become participating physicians include: publication of directories of participating physicians, toll-free telephone lines to disseminate names of participating physicians and use of direct lines for electronic receipt of claims.

c. Noncompliance

Nonparticipating physicians would be subject to penalties for increasing their charges to Medicare beneficiaries during this 15-month period compared with charges they made during the quarter April 1, 1984–June 30, 1984. Noncompliance would subject these physicians to civil monetary penalties (of not more than $2,000 per violation) and/or exclusion from the Medicare program for not to exceed 5 years.

In no circumstances will the exclusion penalty be imposed in the case of the sole physician serving a community or a physician providing essential specialized services that would otherwise not be available.

If either a participating or nonparticipating physician breaks an assignment agreement by extra billing to beneficiaries, the physician would become subject to the same penalties as are provided under existing law.

d. Monitoring

A monitoring system would be established by the Secretary in order to determine compliance of nonparticipating physicians with the fee freeze and to review changes in volume of services provided.

13. Study of Medicare Part B payments (section 2309)

The conference agreement would require the Director of OTA to study and report to Congress by December 31, 1985, on methods by which Medicare Part B payment amounts and program policies may be modified:

(a) To eliminate inequities in the relative amounts paid to physicians by type of service, locality, and speciality, with particular attention to any inequities between cognitive services and medical procedures;

(b) To increase incentives for physicians and other suppliers under such part to accept assignment for Medicare services; and

(c) To examine the influences of payment methodologies and levels on utilization of services.

The report must also include information on methodologies to be applied in the development of national or regional fee schedules for payments which are consistent with the study carried out by the Secretary.

14. Pacemaker reimbursement review and reform (section 2304)

The conference report would require the Secretary to revise the current guidelines on the frequency of transtelephonic monitoring.

The conference agreement would provide that, if the Secretary fails to revise the guidelines by October 1, 1984, a specified frequency schedule would be in effect with respect to single-chamber cardiac pacemakers powered by lithium batteries.

The conference agreement would provide for a registry of pacemaker devices and leads; would authorize the Secretary of HHS to require that removed devices be returned to the manufacturer; and would permit the Secretary to require testing of such devices.

15. Limitation on certain foot-care services (section 2325)

The conference agreement would require the Secretary to deny coverage under the Medicare program for debridement of mycotic toenails if performed more frequently than once every 60 days. Exceptions would be authorized if medical necessity were documented by the billing physician.

16. Presidential appointment and pay level for the Administrator of the Health Care Financing Administration (section 2332)

The conference agreement would provide for the appointment of the Administrator of HCFA by the President with the advice and consent of the Senate. It would increase the position and pay of the Administrator to level IV of the Executive Schedule.

17. Provider representation on Peer Review Organizations (PRO's) (section 2334)

The conference agreement would provide for limited representation of providers on PRO's. It would allow up to 20 percent of the members of a PRO governing body to be affiliated with providers.

The conference agreement would permit entities whose board members include a representative of a self-insured employer to qualify as a PRO. In addition, an organization which has no more than one member affiliated with a health maintenance organization would not be classified as a payer organization and would therefore be permitted to qualify as a PRO.

18. Access to home health services (section 2336)

The conference agreement would permit a physician who has a financial interest in an agency which is a sole community home health agency, as determined by the Secretary, to carry out certification and plan of care functions for patients served by the agency.

The conference agreement would delete from the list of disqualified physicians uncompensated officers or directors of an agency.

19. Repeal of special tuberculosis treatment requirements under Medicare and Medicaid (section 2335)

The conference agreement would repeal the special conditions and requirements currently applicable to tuberculosis hospitals as no longer necessary. It would also eliminate the special provider category for tuberculosis hospitals.

The conference agreement would repeal the requirement that psychiatric hospitals and units be accredited by the JCAH, and permit the provider to also qualify to participate on the basis of accreditation by other organizations approved by the Secretary. (See item 24 below.)

20. Indirect payment of supplementary medical insurance benefits (section 2339)

Under current law, Part B payments generally may not be made to anyone other than a beneficiary or an entity providing services.

The conference agreement would permit Part B payments to be made to a health benefits plan, if the beneficiary agrees and if the physician or other supplier accepts the plan's payment as payment in full.

21. Including podiatrists in definition of "physician" for outpatient physical therapy services and including podiatrists and dentists in the definition of "physician" for outpatient ambulatory surgery (section 2341)

Under current law, outpatient physical therapy services are covered only if the patient is under the care of a physician. The conference agreement would define a podiatrist (when acting within the scope of his practice) as a physician for purposes of the outpatient physical therapy requirement.

The conference agreement would also include dentists and podiatrists within the definition of physician for purposes of outpatient ambulatory surgery in a physician's office.

22. Establishment by physical therapist of plans for physical therapy (section 2342)

Under current law, Medicare payment for outpatient physical therapy services furnished to a beneficiary may be made only if a plan for furnishing such services is established and periodically reviewed by a physician.

The conference agreement would allow either the physical therapist or the physician to establish the plan of care. The physician would still be required to periodically review all plans of care. The provision would apply with respect to plans of care established on or after the date of enactment.

23. Medicare recovery against certain third parties (section 2344)

Under current law, Medicare may limit benefit payments for services for which other third party insurance programs (e.g. worker's compensation, auto or liability insurance, and employer health plans) may ultimately be liable. However, the law does not make it explicit that the Secretary has the right of subrogation, i.e., the right to become a party to claims against other liable parties or to recover directly from such parties.

The conference agreement would establish the statutory right of Medicare to: (1) bring an action directly against certain third parties, if the beneficiary does not do so; (2) bring an action against any party who has already been paid; or (3) join or intervene in an action against a third party.

24. Use of accrediting organizations under Medicare (section 2346)

The conference agreement would extend the Secretary's authority to rely on accrediting organizations in determining whether rural health clinics, laboratories, clinics, rehabilitation agencies, including outpatient rehabilitation facilities, psychiatric hospitals, and public health agencies meet Medicare requirements (and would clarify the Secretary's authority with respect to ambulatory surgical centers.)

25. Confidentiality of accreditation surveys (section 2345)

The conference agreement extends the disclosure protections given the Joint Commission on the Accreditation of Hospitals survey information to similar survey information provided to the Secretary by the American Osteopathic Association or other national accreditation organizations.

26. Payment for services following termination of participation agreements with home health agencies or hospice programs (section 2348)

The conference agreement would change from the end of the calendar year to 30 days after termination, the ending of coverage for services provided under a plan of care established prior to the termination date of the participation agreement.

27. Exclusion of certain entities owned or controlled by individuals convicted of Medicare or Medicaid related crimes (section 2333)

Under present law, the Secretary may bar from participation in Medicare (and may direct State agencies to bar from Medicaid) a person convicted of program-related criminal offenses. The Secretary may refuse either to enter into or renew a provider agreement with an entity in which ownership or control is held by a person so convicted.

The conference agreement would extend the Secretary's authority by authorizing the Secretary to terminate agreements with any entity in which ownership or controlling interest is held by a person convicted of a program-related criminal offense, or an entity in which an officer, director, agent or managing employee was convicted of such a criminal offense.

The conference agreement would: (a) require the Secretary to notify State Medicaid agencies and authorize the Secretary to require such agencies to bar the entity from participation in the program; and (b) require the Secretary to notify the appropriate State licensing or certification agency and request that appropriate investigations be made and that the State agency keep the Secretary and the Inspector General informed of any action taken.

28. Elimination of Health Insurance Benefits Advisory Council (section 2349)

The Social Security Act provides for a 19 member panel of health experts (the Health Insurance Benefits Advisory Council or HIBAC) to be appointed by the Secretary to advise on matters of general policy with respect to the Medicare and Medicaid programs. The panel has been inactive for many years. The conference agreement would repeal the provision.

29. Health Maintenance Organizations and Competitive Medical Plans (section 2350)

Under current law, health maintenance organizations (HMO's) are required to have an annual open enrollment period of at least 30 days during which time they must accept Medicare beneficiaries up to the limits of their capacity. If there is more than one HMO in an area, there is no current requirement that the open enrollment periods be coordinated. In addition, the conference agreement would allow an HMO to establish a benefits stabilization fund for a limited period of time.

The conference agreement would require the Secretary (after consultation with such organizations) to designate a single 30-day period each year in which all of the HMO's in an area participating in Medicare must have an open enrollment period. It would permit HMO's to conduct open enrollment at other times during the year.

The conference agreement would expand the types of providers to whom Medicare can make payments directly for HMO services to include hospitals and skilled nursing facilities.

30. Deadline for report on including payment for physicians' services to hospital inpatients in DRG payment amounts (section 2317)

Present law requires the Secretary to report to the Congress on the advisability and feasibility of making payments for physician services furnished to hospital inpatients based on a diagnosis-related group system and to make legislative recommendations. The report is to be part of the report made to Congress during 1985.

The conference agreement would require the Secretary to report to Congress not later than July 1, 1985.

31. Flexible sanctions for noncompliance with requirements for end-stage renal disease facilities (section 2352)

Under current law, end-stage renal disease (ESRD) facilities that are not in complete compliance with Medicare program requirements are subject to decertification.

The conference agreement would authorize the Secretary to apply intermediate sanctions to such facilities, such as denial of reimbursement for some or all patients admitted after the facility is notified of its noncompliance, or graduated reduction in reimbursement.

32. Emergency room services (section 2318)

Current law requires the Secretary to place reasonable limits on hospital costs and physician charges for outpatient services; bona fide emergency services provided in hospital emergency rooms are specifically exempted by statute from the limits.

The conference agreement would provide a statutory definition of "bona fide emergency services" which would include services provided in a hospital emergency room after the sudden onset of a medical condition manifesting itself by acute symptoms of sufficient severity (including severe pain) such that the absence of immediate medical attention could reasonably be expected to result in: (a) placing the patient's health in serious jeopardy; (b) serious impairment to bodily functions; or (c) serious dysfunction of any bodily organ or part. The provision would be effective with respect to services furnished on or after date of enactment.

33. Part B premium (section 2302)

Currrent law requires the Secretary to calculate and announce each September the amount of the monthly premium that will be charged in the following calendar year for people enrolled in the Supplementary Medical Insurance (Part B) portion of the Medicare program. A temporary provision of law requires that for 1984 and

1985 the premium amount be calculated so as to produce premium income equal to 25 percent of program costs for enrollees aged 65 and over.

Beginning with 1986, the premium calculation under current law will revert to an earlier method under which the premium amount is the lower of: (1) an amount sufficient to cover one-half of program costs for the aged; or (2) the current premium amount increased by the percentage by which cash benefits were most recently increased under the cost-of-living adjustment (COLA) provisions of the Social Security program.

The conference agreement would extend for two years (CY 1986 and 1987) the existing temporary provision which fixes the proportion of the Part B Medicare costs financed by enrollees at 25 percent of program costs. Should no Social Security cost-of-living adjustment take place, the monthly premium would not be increased for that year.

In the case of an individual who has his or her Part B premium deducted from his or her Social Security check, if the cost-of-living adjustment is less than the amount of the increase in the premium, the premium increase would be reduced so as to avoid a reduction in the individual's Social Security check. In certain cases, the monthly premium would not increase for that individual for that year.

Year	Estimated Monthly Premium	
	Current law	Conference agreement
1986	$17.70	$19.10
1987	18.60	21.30

34. Revaluation of assets (section 2314)

Medicare currently reimburses hospitals and other providers for their capital-related costs, including depreciation costs and interest. Investor-owned hospitals also receive a return on equity. When hospitals and other providers are sold, their assets are often revalued, thereby increasing reimbursement for these capital-related costs.

The conference agreement would limit the increase in capital-related cost reimbursement to a new owner that would result from the revaluation of hospital or skilled nursing facility assets. The capital-related cost of the new owner would be based on the lesser of: (a) historical cost (the acquisition cost to the owner of record on the date of enactment), or (b) the purchase price to the new owner.

The Secretary would be required to continue recapture of depreciation as under current reimbursement policy.

The provision would not apply with respect to changes of ownership of assets pursuant to an enforceable agreement entered into before the date of enactment.

The conference agreement excludes from the calculation of allowable costs those expenses (such as lawyers' fees and feasibility studies) related to acquisitions and mergers. The provision is effective for costs incurred on or after the date of enactment.

The conference agreement also limits State medicaid reimbursement for the costs associated with the sale or transfer of a hospital or nursing home. States would be required to assure the Secretary that the methodologies used to establish rates paid to hospitals, SNF's or ICF's can reasonably be expected not to increase those rates more than they would increase under Medicare policy as the result of a change of ownership of a facility.

The provision applies to medical assistance furnished on or after October 1, 1984, except in certain cases requiring State legislation.

35. Elimination of special payment provisions for preadmission diagnostic testing (section 2305)

"The Omnibus Reconciliation Act of 1980" authorized 100 percent Part B reimbursement on a reasonable cost or charge basis for preadmission diagnostic testing, either in a hospital's outpatient department or in a physician's office, within seven days prior to a hospital admission.

The final regulation implementing 100 percent reimbursement for preadmission testing was not published.

The conference agreement would repeal the provision. It would clarify that repeal shall not be construed as prohibiting program payments (subject to cost-sharing) for preadmission diagnostic testing performed in a physician's office to the extent such testing is otherwise reimbursable. The section would be effective with respect to services performed after the date of enactment.

36. Contracts for Medicare claims processing (section 2326)

The conference agreement continues the right of providers to nominate intermediaries, but makes a specific exception for competitively bid contracts.

The Secretary would be required to limit the number of home health regional intermediaries (by the end of three years) to no more than ten, in order to establish expertise in home health claims processing and to facilitate uniform interpretation of Medicare rules.

The conference agreement provides that in determining a carriers, or intermediary's necessary and proper cost of administration, the Secretary shall, with respect to each contract, take into account the amount that is reasonable and adequate to meet the costs which must be incurred by an efficiently and economically operated organization in carrying out the terms of its agreement. It would be required that all carriers and intermediaries perform the full range of carrier or intermediary activities and be health insuring organizations.

The Secretary would be permitted to enter into no more than two competitively bid contracts under part A, and two competitively bid contracts under part B of Medicare, for each of the next two years only. These competitive contracts could only be used to replace consistently poor performers (contractors falling into the lowest 20th percentile of all performers, as measured by published cost and performance criteria).

The conference agreement requires that standards for carriers and intermediaries be available for public comment prior to implementation but does not require that they have to go through the full rulemaking procedures.

37. *Lesser of cost or charges (section 2308)*

Under current law, Medicare pays providers the lesser of costs or charges (LCC). HCFA regulations allow hospitals to calculate the amount of their cost and charges in the aggregate for inpatient and outpatient services.

The conference agreement would require the Secretary to issue regulations to isolate the calculation of the lesser of cost or charges for outpatient services from the calculation for inpatient services.

To protect hospitals serving substantial numbers of indigent patients, the Secretary would be required to modify the current rule under which public providers determined to have nominal charges are exempted from the lesser of cost or charges provision.

The same rule would also apply to nonpublic providers that serve a substantial number of indigent patients.

38. *Coverage of hemophilia clotting factor (section 2324)*

Under current law, Part B of Medicare excludes coverage for drugs and biologicals unless they are of the type that cannot be self-administered and are commonly furnished as incident to physicians' services.

The conference agreement would provide Medicare coverage, subject to utilization controls deemed necessary by the Secretary, for blood clotting factors and the supplies necessary for the self-administration of the clotting factor. The provision would apply to items and services purchased on or after enactment.

39. *Cost-sharing for durable medical equipment furnished as a home health benefit (section 2321)*

Under present law, Medicare payment for durable medical equipment which is not provided as a covered inpatient service is based on 80 percent of reasonable charges (80 percent of reasonable costs in the case of a provider), with one exception. Payment is based on 100 percent of costs when furnished as part of a covered home health service.

The conference agreement would require 20 percent coinsurance on durable medical equipment provided by home health agencies. It also clarifies the definition of durable medical equipment and the coverage of such equipment when furnished by providers.

40. *Modification of working aged provision (section 2301)*

"The Tax Equity and Fiscal Responsibility Act of 1982" (TEFRA) changed the Medicare benefits for the working aged. TEFRA amended "The Age Discrimination in Employment Act" (ADEA) to provide that an employer must offer to an employee age 65 through 69 the same group health plan offered to employees under age 65. As of January 1, 1983, if the employee elects the employer plan, Medicare benefits become secondary to benefits under the employer group health plan for an employed individual between the ages of 65 and 69 (and for the spouse of such employed individual, if the spouse is age 65 through 69).

The conference agreement would provide that employers must also offer group coverage to an employee who has not reached age 65 in cases where the employee has a spouse age 65 through 69 under the same circumstances as coverage is offered to employees with a spouse under the age of 65. In the case where such employee elects the employer plan, Medicare coverage for his older spouse would be secondary.

41. Elimination of Part B deductible for certain diagnostic laboratory tests (section 2303)

Current law authorizes the Secretary to negotiate with a laboratory a payment rate that is considered the full charge for diagnostic tests. The payment, which is made directly to the laboratory, equals 100 percent of the negotiated rate subject to the annual Part B deductible. The beneficiary is not liable for coinsurance payments.

The conference agreement would eliminate application of the annual Part B deductible in the case of diagnostic tests performed in a laboratory which has entered a negotiated rate agreement with the Secretary.

The conference agreement would specify that the current law provision providing for negotiated agreements only applies to services not paid for under the new fee schedule (see Item 9).

42. Repeal of exclusion of for-profit organizations from research and demonstration grants (section 2331)

Current law limits the awarding of grants for the conduct of research and demonstrations to non-profit organizations. Contracts are permitted to be awarded to both for-profit and non-profit organizations.

The conference agreement would extend the research and demonstration grant authority to for-profit organizations.

43. Payments to promote closing and conversion of underutilized hospital facilities (section 2353)

Section 2101 of the "Omnibus Budget Reconciliation Act of 1981" (Public Law 97-35) authorized the Secretary to make Medicare and Medicaid payments to cover capital and increased operating costs associated with the closing or conversion of underutilized hospital facilities.

The conference agreement would require the Secretary to provide to the Congress an analysis of the modifications required to conform the closure and conversion program to the prospective payment system established under Section 1886 of the Act.

44. Judicial review of provider reimbursement review board decisions (section 2351)

The conference agreement would specify that those providers that bring an administrative appeal as a group before the Provider Reimbursement Review Board because of a common issue of fact, law or regulation must then bring any judicial appeal as a group.

The amendment applies to any administrative action or judicial appeal brought on or after enactment.

The conference agreement would clarify that civil action may be taken within 60 days after notification is received (rather than after a determination is rendered) that the Provider Reimbursement Review Board determines it does not have authority to decide a question. The amendment would be effective upon enactment.

The conference agreement clarifies the effective dates of certain provisions of current law by specifying that for actions brought by groups of providers in a judicial area where the largest number of them is located, the effective date would be actions brought on or after April 20, 1983. For actions brought by providers under common ownership, the effective date is the date of enactment of this bill.

45. Enrollment and premium penalty with respect to the working aged provision (section 2338)

The Tax Equity and Fiscal Responsibility Act (TEFRA) required employers to offer their employees aged 65 to 69 the same health benefits plan offered to their younger workers. Medicare payments are secondary with respect to these older workers (and their spouses aged 65–69). (The conference agreement extends the provision to include younger workers; see item 40.) Employees who elect enrollment in such employer-offered health benefit plans, and their spouses, may wish to delay enrollment in Part B because Part B coverage may be duplicative. However, persons who enroll late are currently subject to a penalty. The monthly Part B premium is increased by 10 percent for each full 12 months that an individual delays enrollment in the program beyond his or her initial enrollment period.

The conference agreement would waive the Part B enrollment penalty for workers and their spouses aged 65 through 69 who elect private coverage under the provision of TEFRA and would establish special enrollment periods for such workers. The waiver would apply for the period during which an individual continued to be covered under an employer's group health benefits plan.

The conference agreement would provide that the penalty relief provision would be effective with respect to the first calendar month beginning at least 30 days after enactment.

The conference agreement would provide that the special enrollment provisions would be effective for months beginning more than 90 days after enactment.

46. Waivers for Social Health Maintenance Organizations (section 2355)

The Secretary has general authority to conduct experiments and demonstrations. While the Department has provided start-up funding for a social HMO project, waivers allowing the four demonstration sites to become operational have not been approved by the Office of Management and Budget.

The conference agreement would require the Secretary to approve certain waivers for a project to demonstrate the concept of a social HMO at four sites within 30 days after submission of a waiver request or within 30 days of enactment in the case of waiver requests submitted prior to enactment.

The conference agreement requires submission to Congress of an interim report on the status of the projects within 45 days of enactment. A final report is due to Congress forty-two months after enactment.

47. Peer Review Organizations (PRO's) (section 2347)

Under current law, payment of PRO's is made from the Part A trust fund. The Secretary is directed to fund PRO's in amounts determined to be reasonable, but not less than the 1982 funding levels (adjusted for inflation). This provision does not apply to PSRO's. Public Law 98-21 required hospitals to enter into an agreement with a peer review organization as a condition of payment under the Medicare program. Such agreements must be entered into by October 1, 1984. Health benefit payer organizations may not qualify as a PRO until after October 1, 1984.

The conference agreement would require hospitals, as a condition of Medicare payment, to enter into an agreement with a PSRO in the area and would fund PSRO's out of the Medicare trust fund. The provision would be effective on enactment.

The conference agreement would also delay the date by which hospitals are required to have an agreement with a PRO from October 1, 1984 to November 15, 1984. The date on which health benefit payer organizations can first qualify as PRO's would also be November 15, 1984.

48. Technical amendments relating to Medicare prospective payment (section 2315)

a. Public Law 98-21 provided that hospitals in a State may be reimbursed according to the State's hospital reimbursement control system rather than under prospective payment, provided certain conditions are met. The conference agreement would require approved State systems to prevent unbundling of services and inappropriate admissions practices as is required of hospitals under the prospective payment system.

b. Currently, the Secretary is required to publish in the Federal Register for public comment the proposed annual index and the final annual index of DRG's. The conference agreement would clarify that public comment is required only on the proposed annual index.

c. Under Public Law 98-21, hospitals paid on the basis of the new prospective payment system are required to have an agrement with a peer review organization. The conference agreement would require hospitals exempt from the Federal prospective payment system to have agreements with PRO's or PSRO's.

The conference agreement would clarify that the State program and exempt-hospital provisions of Public Law 98-21 would be effective October 1, 1983. In addition, the conference agreement would require publication of proposed regulations by July 1, 1984, and final regulations by October 1, 1984, with respect to requirements for State systems.

The conference agreement directs the Secretary to develop a definition of hospitals with a "significantly disproportionate number of patients who have low income or are entitled to benefits under Part A" and to identify such providers by December 31, 1984, so that a better determination can be made under existing law as to whether payment adjustments or exceptions are appropriate.

49. Normalization of Trust Fund transfers (section 2337)

The Social Security Amendments of 1983 revised the accounting procedures of the Old Age and Survivors, Disability, and Hospital Insurance Trust Funds to provide that the Treasury would credit to the Trust Funds, at the beginning of each month, the amount of payroll taxes estimated to be received during the month. Under prior law, amounts were paid to the Trust Fund from "time to time."

The conference agreement would repeal the "normalization" provisions with respect to the Hospital Insurance Trust Fund. Thus, funds would be transferred from the Treasury to the HI Trust Fund as under prior law. The provision would not affect the OASDI Trust Funds.

50. Services of a clinical psychologist provided to members of an HMO (section 2322)

Under current law, services of physician assistants and nurse practitioners are recognized as "medical and other health services" if they are furnished pursuant to a risk-sharing arrangement with a health maintenance organization.

The conference agreement would provide that the services of clinical psychologists, when furnished pursuant to a risk-sharing arrangement with a health maintenance organization, are recognized as "medical and other health services."

The Secretary would have the authority to specify the qualifications necessary to be identified as a clinical psychologist.

PART THREE: SUMMARY OF ADDITIONAL SPENDING REDUCTION PROVISIONS WITHIN THE JURISDICTION OF THE COMMITTEE ON FINANCE IN THE SENATE AND THE COMMITTEE ON ENERGY AND COMMERCE IN THE HOUSE

A. Medicaid and Maternal and Child Health Provisions (subtitle B of title III of Division B)

1. Medicaid coverage for pregnant women and young children (section 2361)

Under present law, States must provide medicaid to poor women and children receiving cash assistance under AFDC. They have the option of extending coverage at their current Federal matching rates to, among others, the following additional groups meeting AFDC income and resource requirements: first-time pregnant women; pregnant women in two-parent families where the principal breadwinner is unemployed; pregnant women in two-parent families; and children under age 18 or 21 in two-parent families (Ribicoff children).

The conference agreement requires the States to provide medicaid coverage at regular Federal matching rates to the following groups meeting AFDC income and resources requirements: (1) first-time pregnant women from medical verification of pregnancy; (2) pregnant women in two-parent families where the principal breadwinner is unemployed, from medical verification of pregnancy; and (3) children born on or after October 1, 1983, up to age five in two-parent families.

This provision is effective October 1, 1984, or where the Secretary determines States legislation is necessary, the first day of the first calendar quarter after the close of the first regular legislative session after enactment, whether or not the Secretary issues implementing regulations.

2. Clarification of medicaid entitlement for certain newborns (section 2362)

Under present law, certain States have established medicaid application procedures that fail to provide for the automatic addition of a newborn child to a medicaid beneficiary's family unit for coverage purposes.

The conference agreement provides that a child born to a woman eligible for and receiving medicaid at the time of birth is deemed eligible for up to one year, as long as the woman remains eligible. This provision applies with respect to children born on or after October 1, 1984.

3. Recertification of need for stays in SNFs and ICFs (section 2363)

a. Recertifications

Under present law, a State's evidence of a satisfactory program of controls over utilization must include evidence that physicians (or a physician assistant or nurse practitioner under the supervision of a physician) recertify the need for continued skilled nursing facility (SNF) and intermediate care facility (ICF) services every 60 days. Under the conference agreement, recertifications of SNF patients and ICF patients would become a State Medicaid plan requirement. Such recertifications of SNF patients would be required 30, 60 and 90 days after admission, and every 60 days thereafter. In addition, with respect to ICF, recertifications would be required 60 and 180 days after admission; 12, 18 and 24 months after admission; and annually thereafter.

b. Grace period

The bill permits a 10-day grace period if the state can demonstrate that the physician had good cause for missing the deadline.

c. Penalty

Under present law, the Federal penalty imposed on States which fail to have an adequate utilization control program is 33⅓ percent times the ratio of the number of patients in facilities with one or more records out of compliance to the total number of patients in facilities in the State.

Effective July 1, 1984, the current penalty would not apply to the physician recertification requirement with respect to SNF or ICF patients. However, the current penalty would continue to apply to the requirement that States have an effective program of medical review.

d. Secretarial duty

A U.S. district court has held that the Secretary of Health and Human services has the authority, but lacks the duty, to assure that nursing homes participating in the medicaid program provide care consistent with the individual needs of their medicaid patients. In *re estate of Smith* v. *O'Halloran,* 557 F. Supp. 289 (D. Colo. 1983).

The conference agreement reaffirms the Secretary's existing duty to assure that the standards governing the provision of care to medicaid patients in SNF's and ICF's, and the enforcement of those standards, are adequate to protect the health and safety of the residents and to promote effective and efficient use of public monies.

The provisions (a–d) are effective for calendar quarters on or after enactment, except for SNF admissions before enactment, in which case the amendments would not require recertifications sooner or more frequently than were required under the law in effect before such date.

4. Waiver of certain membership requirements for certain HMO's (section 2364)

Under present law, the number of medicare/medicaid beneficiaries enrolled in a health maintenance organization (HMO) or other prepaid plan delivering services on a risk basis cannot exceed 75 percent of the total enrollment. The Secretary may waive the requirements in the case of public HMO's if the Secretary determines that special circumstances warrant and the entity is making reasonable efforts to enroll non-medicare/medicaid beneficiaries.

The conference agreement permits the Secretary to modify or waive the 75-percent enrollment limitation in the case of an HMO that: (1) is nonprofit; (2) has at least 25,000 enrollees: (3) is and has been a Federally-qualified HMO for at least 4 years; (4) provides basic health services through its staff; (5) is located in a medically underserved area; and (6) had previously received a waiver of the 75 percent limitation under section 1115 of the Act. The Secretary may exercise this waiver only if she determines that special circumstances warrant and that the organization had made, and is making, reasonable efforts to enroll non-medicare/medicaid beneficiaries.

In addition, under current law, medicaid eligibles enrolled in HMO's may disenroll, without cause, upon one month's notice. The conference agreement will permit States to require medicaid beneficiaries who choose to enroll in HMO's meeting certain requirements to remain in the HMO for up to 6 months, unless the beneficiary had good cause to disenroll before that time. During the first month of each 6-month period, the beneficiary could disenroll without cause and receive a medicaid card that did not restrict his or her choice of provider. For the remainder of each 6-month period, the beneficiary would have to satisfy the State that there was good cause for disenrollment, such as poor quality care or lack of access to needed specialty services. States would be expected to establish effective procedures for reviewing requirements for disenrollment on a prompt and fair basis. As under current law, enrollment in HMO's would be voluntary; beneficiaries would have freedom of choice among participating HMO's, and between prepaid and free-service providers.

The conference agreement limits the ability of States to impose these restrictions on beneficiary freedom of choice to the following two types of entities: (1) Federally-qualified HMO's, and (2) organizations that are receiving, and have at least two years prior to contracting with the medicaid program received, grants of at least $100,000 under the Migrant Health Center, Community Health Center, and Appalachian Regional Commission programs. In each case, at least 25 percent of the organization's prepaid patients would have to be other than medicare or medicaid beneficiaries. The States would be required to notify beneficiaries prior to enrollment, and at least twice a year thereafter, of their disenrollment rights. The current Federal regulatory requirements with respect to prepaid HMO contracts, including those relating to grievance procedures and quality assurance systems, would apply to these special "lock-in" arrangements as well.

The provision is effective on the date of enactment.

5. Maximum amount of medicaid payments to Puerto Rico and the Territories (section 2365)

Current law established the following annual ceilings on the amount of Federal medicaid matching payments which certain jurisdictions may receive: Puerto Rico, $45 million; Virgin Islands, $1.5 million; Guam, $1.4 million; Northern Mariana Islands, $350,000; and American Samoa, $750,000.

The conference agreement raises the ceiling to the following levels: Puerto Rico $63.4 million, Virgin Islands, $2.1 million; Guam, $2.0 million; Northern Mariana Islands, $550,000; and American Samoa, $1.15 million. The provision is effective for fiscal years beginning on or after October 1, 1983.

6. *Payment for psychiatric hospital services (section 2366)*

Under present law, special reimbursement limitations apply with respect to hospital inpatients who are awaiting nursing home placement.

The conference agreement delays, until July 1, 1985, the application of reimbursement limitations with respect to public phychiatric hospitals. The conference agreement further provides that the reductions made for the 12-month periods ending June 30, 1986, and June 30, 1987, are one-third and two-thirds, respectively, of the amounts which would otherwise have been required. The provision is effective on July 1, 1985.

7. *Miscellaneous technical amendments (section 2373)*

Titles V and XIX of the Social Security Act contain certain technical errors.

The conference agreement directs the Secretary not to take any compliance, disallowance, penalty or other regulatory action against a State because a State, in determining eligibility for noncash medicaid recipients, is using an income or resource standard or methodology that is less restrictive than the applicable cash assistance standard or methodology. The Secretary is further directed to report to Congress within 12 months of enactment on the impact of the application of income and resource standards and methodologies under the cash assistance programs to medically needy recipients and other noncash eligibles. The moratorium on Secretarial action is to run from the date of enactment until 18 months after the date on which the Secretary submits her report.

In addition, the conference agreement makes technical corrections to Titles V, and XIX of the Social Security Act.

The provisions are effective on the date of enactment.

8. *Mandatory assignment of rights of payment by medicaid recipients (section 2367)*

Under present law, states are permitted to require medicaid applicants to assign to the State their rights to medical support and third party payments for medical care. Approximately 25 States have taken advantage of this option.

The conference agreement mandates that States require medicaid applicants to assign to the State their rights to third party payments as a condition of eligibilty. The provision is effective on October 1, 1984, except where State legislation is required, in which case, it is effective the first day of the first calendar quarter beginning after the close of the first regular session of the State legislature that begins after the date of enactment.

9. Requirements for medical review and independent professional review (section 2368)

Medical review requirements for SNF's and independent professional review requirements for ICF's under medicaid both call for teams of physicians, registered nurses and other appropriate personnel to conduct virtually similar kinds of review.

The conference agreement makes State plan requirements consistent for medical review and independent professional review for both ICF's and SNF's. The conference agreement also corrects a technical error to assure that Christian Science sanitoria are excluded from the revised review requirements. This provision is effective on the date of enactment.

10. Flexibility in setting payment rates for hospitals furnishing long-term care services under medicaid (section 2369)

Under present law, special requirements are provided for the establishment of payment rates for small rural hospitals furnishing skilled nursing or intermediate care facility services under medicaid.

The conference agreement permits States to pay for long-term care services at the designated hospitals either on the basis of the special payment rates provided under current law or on the basis of the same general criteria that are applicable to hospitals and nursing homes. Whatever payment method a State chose would have to be applied to all the hospitals in question. The provision applies to services provided after the date of enactment.

11. Authority of Secretary to issue and enforce subpoenas under medicaid (section 2370)

Under present law, the Secretary is authorized to issue and seek enforcement of subpoenas under medicare to obtain information needed in connection with hearings, investigations, and other matters related to fraud and abuse.

The conference agreement authorizes the Secretary to issue and seek enforcement of subpoenas under medicaid to the same extent allowed under medicare, effective on the date of enactment.

12. Medicaid clinic administration (section 2371)

Under present law, states may cover clinic services under their medicaid programs. Regulations issued by the Department of Health and Human Services limit coverage of clinic services to situations in which services are furnished under the direction of a physician. In certain cases; this physician-direction rule has been interpreted as requiring that clinic administrators be physicians.

The conference agreement provides that the clinic need not be administered by a physician, effective for services provided on or after the date of enactment.

13. Increase in authorization for Maternal and Child Health Block Grant Program (section 2372)

The permanent authorization for the Maternal and Child Health Services (MCH) Block Grant is $373 million. In fiscal year 1983, an additional $105 million was appropriated for the Block Grant, and in fiscal year 1984, an additional $26 million was appropriated.

The conference agreement provides for an increase in the permanent authorization level for the MCH Block Grant to $478 million, effective fiscal year 1984.

The provision applies to fiscal years beginning on or after October 1, 1983.

B. Recovery of Hill-Burton Funds (subtitle C of title III of Division B)

1. Recovery (section 2381)

Under present law, the Federal government is entitled to recover amounts awarded to a facility for construction, modernization, or conversion under Title VI and Title XVI of the Public Health Service Act if, within 20 years, the facility (1) is sold or transferred to a proprietary entity, or (2) undergoes a change in use from that for which the assistance was originally provided.

In the case of facilities that were sold or transferred or underwent a change in use before the date of enactment, the conference agreement provides that the interest penalty will not begin to accrue until 30 days after enactment, but in no case earlier than 180 days from the date of sale, transfer, or change in use.

The conference agreement further authorizes the Secretary to waive recovery altogether in the case of the sale or transfer of a facility to a proprietary entity only if the following requirements are met. First, the new owner or manager must agree to assume and comply with the Hill-Burton "community service" obligation, as implemented by current regulations. Second, the acquiring entity must have established an irrevocable trust, the corpus and income of which are to be used exclusively for the provision of uncompensated services to persons unable to pay in accordance with current regulations. The trust must be established in an amount equal to the greater of (1) twice the cost of the remaining "uncompensated services" obligation of the Hill-Burton facility, including any deficits to be made up, as determined by the Secretary under current regulations; or (2) the amount the Federal government would be entitled to recover, as determined by the Secretary.

2. Liens (section 2381)

Under present law, the Federal recovery right does not constitute a lien upon a Hill-Burton facility prior to judgment.

The conference agreement retains current law with respect to liens.

The Secretary shall have in effect regulations and personnel to place in effect the amendments made by this section not later than the expiration of the 180-day period beginning on the date of the enactment of this section.

C. Uncompensated Services Provided by Skilled Nursing Facilities and Intermediate Care Facilities (subtitle D of title III of Division B)

Study (section 2391)

The conference agreement requires the Secretary to conduct a study to determine whether the current regulations should distinguish between hospitals and nursing homes with respect to compliance with the statutory requirement that a Hill-Burton facility provide a reasonable volume of uncompensated services to persons unable to pay. The study is to be transmitted to the Congress no later than January 1, 1985.

APPENDIX: ESTIMATED BUDGET EFFECTS

Table 1.—Summary Revenue Effect of Tax Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984–1989

[Millions of dollars]

Provision	1984	1985	1986	1987	1988	1989	1984–87
I. Tax Freeze; Tax Reforms Generally	1,467	10,172	17,460	23,390	26,426	28,707	52,489
II. Life Insurance Tax Provisions[1]	−80	−315	−375	−469	−541	−626	−1,239
III. Charitable Deduction Rules; Private Foundation Provisions; Exempt Organizations	−24	−89	−146	−168	−197	−232	−427
IV. Simplification Provisions	99	924	175	208	141	69	1,406
V. Provisions Relating to Employers and Employees and to Retirement	31	471	875	1,095	897	725	2,472
VI. Tax-Exempt Obligations	−73	−231	−359	−536	−756	−744	−1,199
VII. Technical Corrections	(2)	(3)	(3)	(3)	(3)	(3)	(4)
VIII. Highway Revenue Provisions	−152	−102	19	−32	109	−21	−267
IX. Miscellaneous Revenue Provisions	−125	−228	−1,055	−952	−809	−698	−2,360
Total Revenue Effect	**1,143**	**10,602**	**16,594**	**22,536**	**25,670**	**27,180**	**50,875**

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[1] The amounts represent the estimated effects of the life insurance tax provisions assuming that certain temporary provisions enacted in the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), which provide for the taxation of life insurance companies, had been terminated. If these provisions had not been allowed to expire at the end of 1983, the estimates for the provisions in the bill would show increases in fiscal year receipts of $935 million in 1984, $1,050 million in 1985, $1,101 million in 1986, $1,192 million in 1987, and $1,291 million in 1988 (increase of $4,278 million for 1984–87).

[2] Gain of less than $5 million.

[3] Gain of less than $10 million.

[4] Amounts have not been assigned to footnotes for summation purposes. Therefore, totals do not include estimates represented by footnotes.

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984–1989

[Millions of dollars]

Provision	1984	1985	1986	1987	1988	1989	1984–87
I. Tax Freeze; Tax Reforms Generally							
A. Tax Freeze and Related Provisions							
Postponement of finance lease provisions	63	348	862	1,381	1,424	741	2,654
Postponement of increase in amount of used property eligible for investment tax credit		44	104	112	65		260
Postponement of increases in amount of property eligible for expensing	230	399	433	386	−118	−427	1,448
Net interest exclusion		1,024	2,858	3,100	3,366	3,637	6,982
Postponement of increase in foreign earned income exclusion	4	31	80	106	107	79	221
Defer scheduled reductions in maximum gift and estate tax rates		(2)	251	332	381	(2)	583
Windfall profit tax rate on newly discovered oil		5					5
Percentage depletion for secondary and tertiary production after 1983							
Excise tax on distilled spirits		149	311	510	520	535	970
Modification of the manner of paying excise taxes on cigarettes and alcohol products		341	−52	5	5	5	294

Extension of excise tax on communications services			1,168	2,016	803		3,184
Subtotal, tax freeze and related provisions	297	2,341	6,015	7,948	6,553	4,570	16,601
B. Leasing Provisions							
Tax-exempt entity leasing	264	800	1,553	2,840	4,711	6,724	5,457
Treatment of certain motor vehicle operating agreements as leases	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Subtotal, leasing provisions	264	800	1,553	2,840	4,711	6,724	5,457
C. Treatment of Bonds and Other Debt Instruments							
Definitions and technical amendments							
Market discount and discount on short-term obligations	50	307	243	246	249	158	846
Original issue discount on tax-exempt bonds	3	5	7	8	10	13	23
Subtotal, debt instruments	53	312	250	254	259	171	869
D. Corporate Tax Provisions							
Dividends received deduction for debt-financed portfolio stock	(3)	(3)	(3)	(3)	(3)	(3)	(10)
Certain dividends from regulated investment companies	2	5	5	5	5	5	17
Corporate shareholder's basis in stock reduced by reason of extraordinary dividends		140	100	100	100	100	340

Table 2.--Estimated Revenue Effects of Tax Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984-1989—Continued

[Millions of dollars]

Provision	1984	1985	1986	1987	1988	1989	1984-87
Nonliquidating distributions by corporations of appreciated property	2	14	48	101	160	222	165
Capital gains distributed from regulated investment companies and real estate investment trusts			83	89	96	103	172
Certain expenses incurred in connection with short sales	22	32	38	43	48	54	135
Nonrecognition of gain or loss by corporations on options with respect to their stock (warrants)	(2)	(2)	(2)	(2)	(2)	(2)	(10)
Accumulated earnings tax		62	78	33	35	36	173
Repeal of stock for debt exception for purposes of determining income from discharge of indebtedness	(2)	(2)	(2)	(2)	(2)	(2)	(10)
Affiliated groups		5	20	39	39	19	64
Earnings and profits		109	283	270	289	278	662
Net operating loss, etc. carryover rules	(5)	(5)	(5)	(5)	(5)	(5)	(10)
Distribution requirements in the case of a "C" reorganization	(3)	(3)	(3)	(3)	(3)	(3)	(10)
Control requirement in a "D" reorganization	(3)	(3)	(3)	(3)	(3)	(3)	(10)
Collapsible corporations	5	57	196	305	351	382	563
Phaseout of graduated rates for large corporations	70	212	185	190	192	194	657

Golden parachute contracts	(2)	(2)	(2)	(2)	(2)	(2)	(10)
Increase in reduction of certain corporate tax preference items from 15 percent to 20 percent		236	357	400	449	512	993
Subtotal, corporate provisions	101	872	1,393	1,575	1,764	1,905	3,941
E. Partnership Provisions							
Shifting of income, gain, loss, and deduction when partnership interests change	4	111	222	278	340	298	615
Uses of partnerships to change the character and timing of income, gain, loss or deduction:							
Payments to partners for property or certain services		20	51	60	69	78	131
Character of gain or loss on contributed property		24	63	66	67	69	153
Transfers of partnership interests by corporations	(1)	50	50	50	50	50	150
Use of tiered partnerships to alter character of income on exchanges of partnership interests	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Exchanges of like-kind property		82	362	667	788	842	1,111
Use of tiered partnership to achieve step-up in basis of partnership assets	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Allocation of liabilities to limited partners	(11)	(11)	(11)	(11)	(11)	(11)	(10)
Subtotal, partnership provisions	4	287	748	1,121	1,314	1,337	2,160

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984-1989—Continued

[Millions of dollars]

Provision	1984	1985	1986	1987	1988	1989	1984-87
F. Trust Provisions	50	237	390	436	464	488	1,113
G. Accounting Changes							
Premature accruals	138	429	510	491	399	373	1,568
Prepaid expenses	108	243	76	93	112	133	520
Deferred payment transactions	(3)	228	721	1,253	1,789	2,349	2,202
Deferred payments for use of property and services	43	258	486	654	846	887	1,441
Capitalization of construction period interest and taxes		159	235	217	146	106	611
Start-up expenses		23	36	31	26	19	90
LIFO conformity		105	185	200	200	200	490
Subtotal, accounting changes	289	1,445	2,249	2,939	3,518	4,067	6,922
H. Tax Straddles	22	427	152	70	58	45	671
I. Foreign Provisions							
Maintaining the source of U.S. source income	13	60	64	70	76	82	207
Maintaining the character of interest income		67	118	129	142	157	314
Income from factoring trade receivables	(3)	306	534	576	622	673	1,416
Source of transportation income	5	13	17	18	19	20	53

Application of accumulated earnings tax to certain distributions received by U.S.-owned foreign corporations	(2)	(2)	(2)	(2)	(2)	(2)	(10)
Repeal of 30-percent tax on portfolio interest paid to foreign persons	−2	−33	−65	−62	−40	−10	−162
Original issue discount in the case of foreign investors	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Withholding on disposition by foreigners of U.S. real property	44	40	10	10	11	14	104
Use of territories to avoid U.S. tax on foreign investors	(3)	(3)	(3)	(3)	(3)	(3)	(10)
Taxation of certain transfers of property outside the United States			12	127	324	540	139
Amendments relating to foreign personal holding companies	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Coordination of subpart F with foreign personal holding company provisions	(2)	(2)	(2)	(2)	(2)	(2)	(10)
Gain from sale or exchange of stock in certain foreign corporations	(3)	(3)	(3)	(3)	(3)	(3)	(10)
Extension of moratorium on application of research and experimental expense allocation regulation	−61	−127	−66				−254
Ordinary income treatment on disposition of stock of certain foreign corporations under Code section 1248	(2)	(2)	(2)	(2)	(2)	(2)	(10)
Foreign investment companies	(3)	(3)	(3)	(3)	(3)	(3)	(10)
Foreign collapsible corporations	(3)	(3)	(3)	(3)	(3)	(3)	(10)
Stapled stock; stapled entities	(2)	(2)	(2)	(2)	(2)	(2)	(10)

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984–1989—Continued

[Millions of dollars]

Provision	1984	1985	1986	1987	1988	1989	1984–87
Insurance of related parties by a controlled foreign corporation	26	44	46	49	51	54	165
Definition of resident alien	5	10	10	10	10	10	35
Treatment of community property income of nonresident aliens	2	5	5	5	5	5	17
Foreign sales corporations		–62	–62	19	80	131	–105
Subtotal, foreign provisions	32	323	623	951	1,300	1,676	1,929
J. Compliance Provisions							
Provisions relating to tax shelters		26	30	28	24	20	84
Information reporting provisions		20	92	175	232	255	287
Other compliance provisions		11	48	53	56	58	112
Subtotal, compliance provisions		57	170	256	312	333	483
K. Depreciation and Related Provisions							
Depreciation of real property	55	291	786	1,478	2,244	3,043	2,610
Depreciation recapture and installment sales	24	56	212	219	224	234	511
Movies	(3)	(3)	(3)	(3)	(3)	(3)	(10)
Sound recordings	5	10	10	10	10	10	35
Subtotal, depreciation provisions	84	357	1,008	1,707	2,478	3,287	3,156

L. Miscellaneous Reform Provisions							
Tax benefit rule		229	253	274	300	330	756
Interest-free and below-market interest rate loans	44	136	167	188	211	237	535
Limitations with respect to property which is partially used for personal purposes and luxury automobiles	48	150	233	269	279	286	700
Transfers of depreciable property between related parties	(2)	(2)	(2)	(2)	(2)	(2)	(10)
Treatment of certain related party transactions	46	109	176	253	346	416	584
Losses on sales and exchanges of property used in a trade or business		27	75	99	131	173	201
Use of multicompany structure to reduce tax on coal operations		2	10	15	17	18	27
Modification of income averaging	133	1,994	1,886	2,053	2,226	2,404	6,066
Taxation of the Federal Home Loan Mortgage Corporation		67	109	142	185	240	318
Interest on debt used to purchase or carry tax-exempt obligations of related parties	(2)	(2)	(2)	(2)	(2)	(2)	(10)
Subtotal, miscellaneous reform provisions	271	2,714	2,909	3,293	3,695	4,104	9,187
Total, tax freeze; tax reforms generally	**1,467**	**10,172**	**17,460**	**23,390**	**26,426**	**28,707**	**52,489**
II. Life Insurance Tax Provisions [6]	**−80**	**−315**	**−375**	**−469**	**−541**	**−626**	**−1,239**

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984-1989—Continued

[Millions of dollars]

Provision	1984	1985	1986	1987	1988	1989	1984-87
III. Charitable Deduction Rules; Private Foundation Provisions; Exempt Organizations							
A. Charitable Deduction Rules							
Nonoperating (grantmaking) foundations		−10	−17	−18	−21	−24	−45
Expansion of circumstances in which a deduction may be claimed for a qualified conservation contribution	(4)	−5	−5	−5	−5	−5	−15
Charitable expense deduction for use of passenger automobile		−5	−37	−43	−51	−60	−85
Subtotal, charitable deduction rules		−20	−59	−66	−77	−89	−145
B. Private Foundation Provisions		−23	−29	−29	−29	−29	−81
C. Exempt Organizations							
Acquisition indebtedness of certain educational institutions	−24	−46	−58	−73	−91	−114	−201
Exemption from UBIT for certain gambling income	(7)	(7)	(7)	(7)	(7)	(7)	(10)
Tax treatment of certain non-profit child care organizations	(4)	(4)	(4)	(4)	(4)	(4)	(10)

Church audits							
Subtotal, exempt organizations	−24	−46	−58	−73	−91	−114	−201
Total, charitable, etc	**−24**	**−89**	**−146**	**−168**	**−197**	**−232**	**−427**
IV. Tax Simplification Provisions							
A. Individual Estimated Tax	(4)	746	−6	−9	−15	−21	731
B. Domestic Relations							
Treatment of transfer of property between spouses or incident to divorce	(4)	(4)	(4)	(4)	(4)	(4)	(10)
Alimony		2	12	33	57	77	47
Dependency exemption	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Innocent spouse relieved of liability in certain cases	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Gift and estate tax liability for transfers of property to spouses incident to divorce	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Subtotal, domestic relations		2	12	33	57	77	47
C. At-risk Provisions	(1)	(1)	(1)	(1)	(1)	(1)	(10)
D. Administrative Provisions							
Miscellaneous Treasury administrative provisions	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Distilled spirits administrative provision	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Financial accounting for the investment tax credit							
Subtotal, administrative provisions	(1)	(1)	(1)	(1)	(1)	(1)	(1)

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984–1989—Continued

[Millions of dollars]

Provision	1984	1985	1986	1987	1988	1989	1984–87
E. Tax Court Provisions							
Annuities for survivors of Tax Court Judges	(9)	(9)	(9)	(9)	(9)	(9)	(10)
Tax Court Commissioners and jurisdictional limit for small tax cases							
Publicity of Tax Court proceedings							
Subtotal, Tax Court provisions	(9)	(9)	(9)	(9)	(9)	(9)	(10)
F. Simplification of Income Tax Credits	100	183	179	194	110	25	656
G. Miscellaneous Simplification							
Preferred stock eligible under section 1244	(4)	(4)	(4)	(4)	(4)	(4)	(10)
Medical expense deduction for certain lodging	–1	–7	–10	–10	–11	–12	–28
Subtotal, miscellaneous simplification	–1	–7	–10	–10	–11	–12	–28
H. Deadwood							
Total, tax simplification	**99**	**924**	**175**	**208**	**141**	**69**	**1,406**

V. Provisions Relating to Employers and Employees and to Retirement							
A. Pension Plan Provisions							
Provisions relating to top-heavy plans	(5)	(5)	(5)	(5)	(5)	(5)	(10)
Distribution rules of qualified pension plans	(2)	(2)	(2)	(2)	(2)	(2)	(10)
Treatment of distributions of benefits substantially all of which are derived from employee contributions	(1)	1	2	2	4	6	5
Repeal of estate tax exclusion for qualified plan benefits			50	50	50	50	100
Affiliated service groups and employee leasing arrangements	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Determination of whether there is a collective bargaining agreement	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Standards for cash-or-deferred arrangements	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Treatments of certain medical, etc., benefits under pension plans	(3)	(3)	(3)	(3)	(3)	(3)	(10)
Limits on contributions and benefits under qualified plans			17	64	106	115	81
Applications of cash-or-deferred arrangement rules to pre-ERISA money purchase pension plans	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Elimination of retroactive application of amendments made by Multiemployer Pension Plan Act of 1980	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Treatment of certain distributions from a qualified termination plan	(1)	(1)	(1)	(1)	(1)	(1)	(10)

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984-1989—Continued

[Millions of dollars]

Provision	1984	1985	1986	1987	1988	1989	1984-87
Special rule for Trans-Alaskan Pipeline employees	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Distribution requirements for plans, accounts, and annuities of an insurer in rehabilitation proceedings	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Extension of time for repayment of qualified refunding loans	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Pension portability involving telecommunications divestiture	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Subtotal, pension plans		1	69	116	160	171	186
B. Welfare Benefit Plans [13]	63	188	217	222	242	280	690
C. Employee Benefits							
Exclusion for certain employer provided fringe benefits; moratorium	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Qualified tuition reduction	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Cafeteria plans	−32	−40	−4				−76
Incentive stock options	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Certain section 83(b) elections	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Employee and welfare benefit fund treated as related persons	(1)	(1)	(1)	(1)	(1)	(1)	(10)

Alimony treated as compensation for IRA purposes	(4)	(4)	(4)	(4)	(4)	(4)	(10)
Subtotal, employee benefits	−32	−40	−4	(4)	(4)	(4)	−76
D. Employee Stock Ownership Provisions		322	593	757	495	274	1,672
Total, provisions relating to employers and employees, etc	**31**	**471**	**875**	**1,095**	**897**	**725**	**2,472**
VI. Tax-Exempt Obligations							
Mortgage subsidy bonds and mortgage credit certificates	−48	−217	−498	−810	−1,017	−1,000	−1,573
Private activity bonds; misc. provisions	−25	−14	139	274	261	256	374
Total, tax-exempt obligations	**−73**	**−231**	**−359**	**−536**	**−756**	**−744**	**−1,199**
VII. Technical Corrections	(2)	(3)	(3)	(3)	(3)	(3)	(10)
VIII. Highway Revenue Provisions							
Reduction in heavy vehicle use tax and increase in diesel fuel tax	−152	−51	84	37	183	52	−82
One-year extension of refund of taxes on fuels used by taxicabs		−2	(1)				−2
Excise tax exemption for certain piggyback trailers		−5					−5
Increase in excise tax exemptions for alcohol fuels mixtures and alcohol fuels; income tax credit for qualified alcohol fuels; and duty on imported alcohol fuels		−44	−65	−69	−74	−73	−178
Total, highway revenue provisions	**−152**	**−102**	**19**	**−32**	**109**	**−21**	**−267**

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984–1989—Continued

[Millions of dollars]

Provision	1984	1985	1986	1987	1988	1989	1984–87
IX. Miscellaneous Revenue Provisions							
A. Estate and Gift Tax Provisions							
Qualification of certain holding company stock for installment payment of estate tax	(4)	–13	–19	–24	–29	–36	–56
Clarification that certain usufruct interests qualify for estate tax marital deduction	(4)	(4)	(4)	(4)	(4)	(4)	(10)
Special estate tax credits	–22						–22
Perfection of estate tax current use valuation elections	(1)	(1)	(1)	(1)	(1)	(1)	(10)
No gain recognized from net gifts made before March 4, 1981	(4)	(4)	(4)	(4)	(4)	(4)	(10)
Reformation of certain charitable split-interest trusts	(4)	(4)	(4)	(4)	(4)	(4)	(10)
Alternate valuation date election		10	10	10	10	10	30
Subtotal, estate and gift provisions	–22	–3	–9	–14	–19	–26	–48
B. Excise Tax Provisions							
Excise tax on sport fishing equipment		12	13	14	14	15	39
Excise tax on certain arrows		(1)	(1)	(1)	(1)	(1)	(10)

Exemption of certain helicopter operations from aviation excise taxes	−3	−4	−4	−5	−2		−16
Superfund excise tax corrections							
Subtotal, excise tax provisions	−3	8	9	9	12	15	23
C. Income Tax Credits							
Definition of new property for tax credit purposes	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Extension of targeted jobs tax credit		−147	−380	−308	−160	−93	−835
Earned income credit [8]		−13	−373	−342	−315	−290	−728
Alternative test for definition of qualified rehabilitated building	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Subtotal, income tax credits		−160	−753	−650	−475	−383	−1,563
D. Capital Gains and Losses	(5)	(5)	−279	−268	−286	−280	−547
E. Miscellaneous Housing Provisions							
Disaster loss deduction for condemned residences	−15	−12	−12	−13	−13	−14	−52
Deductibility of mortgage interest and taxes paid out of tax-free allowances for ministers		(4)	(4)				
Rollover of gain on sale of residence for military personnel stationed overseas	(1)	−5	−5	−5	−5	−5	−15
Treatment of home won in local radio contest and specially designed for handicapped foster child	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Subtotal, miscellaneous housing provisions	−15	−17	−17	−18	−18	−19	−67

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984–1989—Continued

[Millions of dollars]

Provision	1984	1985	1986	1987	1988	1989	1984–87
F. Extensions and Miscellaneous Transition Rules							
Investment income from S corporations	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Extension of the Payment-in-Kind Tax Treatment Act of 1983	–7	–8	15	(1)	(1)	(1)	(10)
Transitional rule for safe-harbor leasing of coal gasification facilities		–8	–2	–1	–1	(1)	–11
Provisions of Indian Tribal Government Tax Status Act of 1982 made permanent	(4)	(4)	(4)	(4)	(4)	(4)	(10)
Amortization of low-income housing rehabilitation expenditures	–2	–7	–18	–32	–43	–34	–59
Disallowance of deduction for costs of demolishing structures	(2)	(2)	(2)	(2)	(2)	(2)	(10)

Reinstatement of deduction for elimination of certain barriers to the handicapped and the elderly	−8	−16	−7				--31
Subtotal, extensions and transitions	−17	−39	−12	−33	−44	−34	−101
G. Additional Provisions							
Employee tips	(1)	(1)	(1)	(1)	(1)	(1)	(10)
FUTA treatment of tips			18	28	30	32	46
FUTA treatment of certain fishing activities	−1	−1					−2
Taxation of unemployment compensation for pre-1978 periods	(7)	(7)					(10)
Tax exemption for the National Credit Union Administration Central Liquidity Facility	(4)	(4)	(4)	(4)	(4)	(4)	(10)
Exclusion from gross income for cancellation of certain student loans	(4)	(4)	(4)	(4)	(4)	(4)	(10)
Duck stamps	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Boundary Waters Canoe Act payments	(1)	(1)					
Tax treatment of regulated investment companies	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Social security treatment of certain church employees [12]	−67	−16	−12	−6	−9	−3	−101

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984-1989—Continued

[Millions of dollars]

Provision	1984	1985	1986	1987	1988	1989	1984–87
Coverage of employees under social security and Federal retirement systems [12]	(1)	(1)	(1)	(1)	(1)	(1)	(10)
Subtotal, additional provisions	−68	−17	6	22	21	29	−57
Total, miscellaneous revenue provisions	−125	−228	−1,055	−952	−809	−698	−2,360
Total, Revenue Effect	1,143	10,602	16,594	22,536	25,270	27,180	50,875

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[1] Negligible.

[2] Gain of less than $5 million.

[3] Gain of less than $10 million.

[4] Loss of less than $5 million.

[5] Loss of less than $10 million.

[6] The amounts represent the estimated effects of the life insurance tax provisions assuming that certain temporary provisions enacted in the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), which provide for the taxation of life insurance companies, had been terminated. If these provisions had not been allowed to expire at the end of 1983, the estimates for the provisions in the bill would show increases in fiscal year receipts of $935 million in 1984, $1,050 million in 1985, $1,101 million in 1986, $1,192 million in 1987, and $1,291 million in 1988.

[7] Loss of less than $1 million.

[8] The changes to the earned income credit will reduce revenues by $4 million in 1985, $116 million in 1986, $105 million in 1987, $98 million in 1988 and $90 million in 1989, and increase outlays by $9 million in 1985, $257 million in 1986, $237 million in 1987, $217 million in 1988, and $200 million in 1989.

[9] Increases budget outlays by a negligible amount.

[10] Amounts have not been assigned to footnotes for summation purposes. Therefore, totals do not include estimates represented by footnotes.

[11] Included in other partnership provisions.

[12] These items appear in Title VI of the Spending Reduction Act of 1984. However, because there are revenue effects associated with the provisions, they are included in the revenue tables.

[13] This includes amounts attributable to changes in the treatment of accrued vacation pay.

Table 3.—Outlay Impact of Certain Spending Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984–1987

[Millions of dollars; negatives indicate spending reductions]

Provision	Category	1984	1985	1986	1987	4-year total
Medicare						
1. Delay implementation of single limit for SNFs	Medicare	20	30	35	40	125
2. Hospital rate of increase	Medicare	0	−160	−420	−520	−1,100
3. Establish fee schedule for clinical lab services.	Medicare	−40	−240	−300	−380	−960
	Medicaid	−10	−49	−57	−67	−183
4. Hepatitis B Vaccine	Medicare	3	−1	−2	−2	−2
5. Physician fee freeze	Medicare	−40	−720	−840	−950	−2,550
	Medicaid	0	−14	−16	−18	−48
6. Limitation on certain foot care services	Medicare	−3	−11	−11	−12	−37
7. Part B premium increase	Medicare	0	0	−384	−884	−1,268
	Decrease in spending reduction due to other savings.	0	187	246	288	721
	Medicaid	0	−14	10	45	41
	Subtotal	0	173	−128	−451	−506

8. Revaluation of assets	Medicare	−2	−25	−45	−70	−142
9. Competitive contracting	Medicare	0	−15	−25	−33	−73
10. Lesser of costs and charges	Medicare	0	−45	−55	−65	−165
11. Coinsurance for DME	Medicare	−5	−20	−25	−25	−75
12. Working aged	Medicare	0	−260	−380	−415	−1,055
Totals	Medicare	−67	−1,467	−2,068	−2,432	−6,034
	Medicaid	−10	−77	−63	−40	−190
	Premiums	0	187	−138	−596	−547
Grand total—Medicare provisions		−77	−1,357	−2,269	−3,068	−6,771
Public Assistance						
1. Increase resource limits in SSI	SSI	0	3	15	30	48
	Medicaid	0	2	10	15	27
	Food stamps	0	0	−5	−5	−10
	Subtotal	0	5	20	40	65
2. Limitation on recoupment rate in case of overpayments.	SSI	0	22	2	2	26
3. Limit overpayment for assets	SSI	0	2	2	2	6
4. Adjustments in SSI and OASDI benefits on account of retroactive benefits	SSI	0	−12	−17	−18	−47
	Food stamps	0	2	4	4	10
	Subtotal	0	−10	−13	−14	−37

Table 3.—Outlay Impact of Certain Spending Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984-1987—Continued

[Millions of dollars; negatives indicate spending reductions]

Provision	Category	1984	1985	1986	1987	4-year total
5. Exclusion of Alaska bonus payment	SSI	0	1	1	1	3
6. Set gross income limit at 130% of poverty	AFDC	0	5	10	10	25
	Medicaid	0	5	15	15	35
	Food stamps	0	0	-5	-5	-10
	Subtotal	0	10	20	20	50
7. Increase standard deduction for part-time work	AFDC	0	20	20	20	60
	Medicaid	0	5	15	15	35
	Food stamps	0	-10	-10	-10	-30
	subtotal	0	15	25	25	65
8. Continue $30 beyond four months	AFDC	0	15	15	15	45
	Medicaid	0	5	10	10	25
	Food stamps	0	-5	-10	-10	-25
	Subotal	0	15	15	15	45
9. Provide $10 per month and medicaid for loss of 30 and ⅓	Medicaid	0	40	40	40	120

10. Make monthly reporting/accounting optional	AFDC	0	0	0	0	0
11. Disregard EITC as income	AFDC	0	8	3	3	14
	Food stamps	0	−4	−1	−1	−6
	Subtotal	0	4	2	2	8
12. Exempt burial plots	AFDC	0	3	3	3	9
13. Reimburse CWEP expenses	AFDC	0	5	5	5	15
14. Permit pilot projects on integrated service delivery	AFDC	0	0	2	2	4
15. Clarify definition of earned income	AFDC	−5	−24	−24	−24	−77
16. Include all adults and children in AFDC assistance unit	AFDC	0	−45	−50	−55	−150
	Medicaid	0	90	115	125	330
	Total	0	45	65	70	180
Totals	SSI	0	16	3	17	36
	AFDC	−5	−13	−16	−21	−55
	Medicaid	0	147	205	220	572
	Food stamps	0	−17	−27	−27	−71
Grand total—public assistance		−5	133	165	189	482

Table 3.—Outlay Impact of Certain Spending Provisions of H.R. 4170 as Passed by the House and the Senate, Fiscal Years 1984-1987—Continued

[Millions of dollars; negatives indicate spending reductions]

Provision	Category	1984	1985	1986	1987	4-year total
Limitation on Excise Tax Rebates to Puerto Rico		0	−185	−276	−296	−757
Grace Commission Recommendations						
1. Verify resources and unearned income	SSI	0	5	−75	−105	−175
	AFDC	0	0	−25	−15	−40
	Medicaid	0	0	−210	−240	−450
	Food stamps	0	0	−40	−50	−90
	Subtotal	0	5	−350	−410	−755
2. Offset general debts against IRS refunds		0	0	−300	−500	−800
3. Accelerate deposit and collection of Federal non-tax receipts		0	0	−800	−800	−1,600
4. To improve the administration of the earnings test	OASI	0	−22	−15	−15	−52
Total—Grace Commission		0	−17	−1,465	−1,725	−3,207
Medicaid						
1. Child Health Assurance Program	Medicaid	0	40	90	140	270
2. Recertification of SNF/ICF patients	Medicaid	−1	−6	0	1	−6
	Medicare	−4	−27	−29	−31	−91

3. Increase Medicaid payment for territories	Medicaid	20	20	20	20	80
4. Payment for psychiatric hospital services extension of Medicaid	Medicaid	3	10	6	3	22
5. Assignment of rights of payment by Medicaid recipients	Medicaid	0	–7	–7	–8	–22
6. Revaluation of assets	Medicaid	–2	–20	–40	–55	–117
Totals—Medicaid provisions	Medicaid	20	37	69	101	227
	Medicare	–4	–27	–29	–31	–91
Other Provisions						
1. Recovery of Hill-Burton Fund		–5	–20	–20	–10	–55
2. Increased authorization for maternal and child health		49	50	38	10	147
Subtotal—Other		44	30	18	0	92
Total Outlay Savings of All Provisions		**–22**	**–1,386**	**–3,787**	**–4,830**	**–10,025**

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